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June 26, 2009

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St., 27th Floor
Toronto ON M4P 1E4

Dear Ms. Walli:

Re: EB-2008-0235 London Hydro 2009 Rates Rebasing Application – LPMA Final Argument

Pursuant to Procedural Order # 3 dated June 10, 2009, please find attached two hard copies of the final argument of the London Property Management Association (LPMA) in the above noted proceeding. An electronic copy has also been filed through the Board's RESS system.

Sincerely,

Randy Aiken
Aiken & Associates

cc: David B. Williamson, London Hydro (courier & e-mail)
James C. Sidlofsky, Borden Ladner Gervais LLP (e-mail)
Intervenors (e-mail)

EB-2008-0235

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 **London Hydro Inc.** for an order approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2009.

LONDON PROPERTY MANAGEMENT ASSOCIATION ("LPMA")

ARGUMENT

June 26, 2009

LONDON HYDRO INC.
2009 RATES

EB-2008-0235

ARGUMENT OF LONDON PROPERTY MANAGEMENT ASSOCIATION

INTRODUCTION

This is the Argument of the London Property Management Association ("LPMA") related to the setting of 2009 rates for London Hydro Inc. ("London Hydro") effective May 1, 2009.

This Argument has been structured to reflect the major components of the London Hydro evidence. Where readily available, LPMA has attempted to provide the impact of its submissions on the revenue requirement of London Hydro. However, in order to minimize intervenor time and costs, a comprehensive impact analysis has not been undertaken. If the Board accepts any or all of the LPMA submissions, it is assumed that the direct and indirect impacts will be determined by London Hydro and reviewed by intervenors and Board Staff through the associated draft rate order. An example of a comprehensive impact analysis would include the direct impact on rate base of a reduction in $10,000 in OM&A expenses or a $25,000 reduction in capital expenditures. Depreciation expense would also be directly impacted by the capital expenditure change. The indirect impacts would include the change in total cost of capital and taxes (due to CCA, interest and OM&A expense changes) and the change in the working capital allowance.

London Hydro is forecasting a significant deficiency. As shown in Exhibit 7, page 5, the gross revenue deficiency is $7,943,577 on forecasted revenues of $56,165,076. The deficiency represents an increase in total revenues of more than 14%. As part of the responses to the original and supplemental interrogatories, London Hydro has made a number of proposed changes to the various components of the revenue requirement. Based on these changes, the revised gross revenue deficiency is $7,674,877, or an

increase in revenues of 13.7%. The revised gross revenue deficiency is found in Exhibit 1, Table 4 at page 22 of the London Hydro Argument-in-Chief dated June 15, 2009.

ADJUSTMENTS TO THE COST OF SERVICE APPLICATION

As noted above, on June 15, 2009 London Hydro filed a number of tables reflecting changes to the revenue deficiency as part of its Argument-in-Chief. LPMA accepts the impacts shown in these tables as being appropriate except where noted in this Argument.

EFFECTIVE DATE OF RATE CHANGE

London Hydro has requested that an Order or Orders approving the proposed distribution rates and other charges to be effective May 1, 2009, or as soon as possible thereafter (Exhibit 1, page 4).

London Hydro filed their rate application in December, 2008, rather than in August, 2009. As a result they were late in filing by approximately 4 months.

As shown in the response to LPMA Interrogatory #1, London Hydro only requested rates be made interim as of May 1, 2009 under the assumption that rate orders are generally issued for 1 year time frame and that the 2008 rates were effective only until April 30, 2009. This does not mean that London Hydro was requesting that the new 2009 rates would be effective May 1, 2009, given the lateness in filing.

In fact, as shown on pages 27 & 28 of Exhibit 1, London Hydro understood that the deferral of filing is application to December 2008 may result in an effective date of September 1, 2009 for its requested rate order. However, London Hydro did indicate that if the OEB was able to process the application that would result in an earlier effective date it should do so. LPMA submits that with reply argument from London Hydro scheduled for mid-July it may be that the final rate order may not be in place by September 1, 2009. Following the Board's Decision in this matter, the Board has typically allowed for 14 days following the Decision for the utility to provide a draft rate order and then a further 7 days for intervenors and Board Staff to review the draft rate

order and provide comments, if necessary. The utility is then provided with a further 7 days to respond to the comments received and make changes as necessary. In other words, assuming a Board Decision is not made before the beginning of August, it is not likely that rates could be in place by September 1. If this is the case, LPMA submits that the rates should effective the first day of the month following when the final rate order has been approved.

LPMA further notes that London Hydro is not requesting a rate rider to cover incremental distribution revenues that would otherwise be recovered during the May – August 2009 period (Exhibit 1, page 28). However, the evidence then goes on to state that its new rates should have an effective date of no later than September 1 2009 and in the event that the OEB is not able to issue a final Rate Order for implementation by September 1, 2009 that the OEB provide for the recovery of incremental revenues for the period of September 1, 2009 to the effective date of the final Rate Order either by way of a further Interim Order approving the proposed distribution rates and other charges effective September 1, 2009 or through an appropriate rate rider that would be in effect from the effective date of the Rate Order through April 30, 2010.

LPMA submits that the Board should reject this proposal if the final Rate Order cannot be implemented on September 1, 2009. In its June 1, 2009 Decision for Peterborough Distribution Inc. ("PDI") in EB-2008-0241, the Board stated that PDI filed its application almost two months after the Board's established filing date of August 15, 2008. In this case the Board found that the new rates would be effective the same date as the implementation date, which it determined would be July 1, 2009. For clarity, the Board indicated that there would be no recovery of any foregone distribution revenue from May 1, 2009 to the implementation date of July 1, 2009. LPMA submits that the Board should follow the same course for London Hydro. If an implementation date of September 1, 2009 can be achieved, then this should also be the effective date for the new rates. However, if the implementation date is later than September 1, 2009, then the new rates should be effective as of the implementation date. There should be no retroactive

increase in rates to September, 2009 and no rate rider to recover the foregone revenues from September 1, 2009 to the implementation date.

RATE BASE

a) Working Capital

LPMA accepts the approach taken by London Hydro to calculate the working capital allowance component of rate base, with the adjustments noted below. However, LPMA continues to believe that the 15% methodology may be overstating the required allowance for working capital and recommends that the Board direct London Hydro to prepare a working cash (lead lag) study for its next rebasing application. LPMA notes that in other Decisions by the Board for 2009 rates of other distributors the Board has noted the expense involved in doing a lead lag study. However, LPMA submits that for a distributor the size of London Hydro this should not be an issue. As shown on page 24 of their Argument-in-Chief, the working capital allowance for London Hydro accounts for just under 20% of total rate base. LPMA submits that the working capital allowance is a significant contributor to the overall revenue requirement of the distributor. A lead lag study should be done to confirm or re-estimate the size of the working capital allowance given its significant impact on the revenue requirement for London Hydro's next rebasing application.

i) Cost of Power

London Hydro used the most recent available OEB RPP price forecast at the time of filing its application to determine the working capital allowance calculation (LPMA Interrogatory #11d). The response to that interrogatory also indicates that London Hydro does not believe there is any logic or rational behind specifying the use of the RPP prices at the Decision date versus the filing date of an application. LPMA agrees with London Hydro unless there is a significant change in the RPP price. It is LPMA's understanding that the current RPP price is less than 1% different from the $0.6030'kWh priced used by London Hydro in its application. As a result of this small difference, LPMA submits that there is no need to update the cost of power component of the working capital allowance calculation.

ii) Changes to Controllable Expenses

LPMA submits that if the Board makes any adjustments to the controllable OM&A expenses in its Decision, these changes should be reflected in the calculation of the working capital component of rate base.

b) Capital Expenditures

London Hydro's capital expenditure forecast for 2009 is $30,572,005 (Exhibit 2, Table 6). This is significantly higher that the capital expenditures in any of the previous years shown for 2005 through 2008. The forecast for 2008 was $20,532,259, and was the highest figure in 2005 through 2008. As shown in the response to LPMA Interrogatory #9a, actual capital expenditures in 2008 totaled $23,358,935. The forecast for 2009, therefore, represents an increase of more than $7.2 million or nearly 31% over the actual 2008 levels.

When combined with the change in CWIP, shown in Table 6 of Exhibit 2, the total capital spending for 2009 is forecast to total $27.43 million. Table 17 of Exhibit 2 shows that this capital spending is $3 to $4 million higher than that forecast for 2010 and 2011. The average of the 2009 through 2011 forecast is $25.061 million. The 2009 forecast is $2.369 above this average.

Most of the increase in capital expenditures in 2009 from the 2008 forecast and the 2008 actual level of expenditures are related to computer software. The forecasted level of expenditures in this category was $460,000 for 2008, while the actual level came in at t under $450,000. The forecast for 2009 is approximately $9,280,000, an increase of about $8.8 million.

London Hydro indicates that it has completed a number of upgrades to its existing software applications over the past five years, including replacing its Customer Information System, Geographic Information System, Document Management System, and an Enterprise Resource Planning system (Exhibit 2, page 18-19).

Expenditures forecast for 2009 include an enhancement to the Customer Information System and new projects related to Mobile Workforce Management (MWM") and an Outage Management System ("OMS"). The costs associated with the latter two projects are $350,000 and $818,000, respectively (Exhibit 2, page 74), for a total of $1.168 million.

LPMA submits that the Board should reduce the capital expenditures for 2009 by $2.369 million to reflect that the forecast for 2009 through 2011 is $25.061 million. Half of this reduction could come from the software projects noted above as they should be delayed to 2010. LPMA submits that there is adequate room to reduce the capital expenditures associated with distribution and general plant by the remaining $1.2 million as this figure represents only about 5% of the total distribution and general plant expenditures forecast for 2009.

OM&A EXPENSES

OM&A expenses at London Hydro have increased dramatically between 2004 and 2008 as reported by London Hydro. The increase in 2009 as compared to actual 2008 expenses is even more substantial.

a) Overall Increase in OM&A Costs

As shown in the response to LPMA Interrogatory #32, the increase in OM&A expenses between 2004 and 2008 was 22.7% in total, or an average annual increase of 5.7%. The increase in 2009 over the actual 2008 expenses is a further 6.8% or $1,790,710, for a total 2009 expense of $28,169,400. Note that all of these figures exclude amortization expense, charitable donations and CDM third tranche spending.

LPMA submits that the increase in 2009 is excessive given substantial increases that have already taken place since 2004. The historical increases have been well in excess of inflation which averaged less than 2.2% over this period (LPMA Interrogatory #35). The forecast for 2009 is again well in excess of inflation. London Hydro has not presented

any evidence to support an increase in OM&A costs in 2009 at a rate that is in excess of its historical average increases in 2004 through 2008.

At the historical increase of 5.7% for the 2004 through 2008 period applied to actual 2008 expenses, the 2009 forecast for OM&A expenses would be capped at $27,882,276, a reduction of $287,124 from that forecast by London Hydro. This figure is confirmed in the response to LPMA Interrogatory #51.

LPMA submits that this figure of $27,882,276 is the maximum OM&A expenses that the Board should approve for London Hydro. As indicated in the following section, LPMA submits that significantly larger OM&A reductions from that forecast should be applied.

b) Specific OM&A Reductions

As the following sections will demonstrate, LPMA submits that significantly larger OM&A reductions from that forecast by London Hydro for 2009 are appropriate.

i) 2009 Rate Rebasing Costs

London Hydro had forecast a total cost associated with the 2009 rate rebasing application of $291,400 (LPMA Interrogatory #38). London Hydro has included one-fourth of this amount, or $72,850 in the 2009 revenue requirement. LPMA agrees with the recovery of these costs over a four year period since base rates determined in this case will be used for the current rebasing year and the following three years under IRM.

At Paragraph 34 of its Argument-in-Chief, London Hydro has reduced the cost associated with the rates rebasing from $291,400 to $220,854 to reflect that there was no technical conference or oral hearing required, but that there was a second round of interrogatories. Amortizing this expense over four years reduces the amount included in the revenue requirement from $72,850 to $55,213 for a reduction of $17,637.

Based on the response to LPMA Interrogatory #38b, LPMA accepts the reduction in these costs as appropriate and submits that the Board should accept the decrease.

ii) Insurance Costs

LPMA submits that the cost associated with insurance costs should be reduced from $501,000 to $444,897 for a total reduction of $56,103. This reduction is based on the response to LPMA Interrogatory #37 in which London Hydro indicated that the cost for insurance for 2009 is $444,897, significantly lower than their forecast of $501,000. London Hydro goes on to indicate that the premiums related to insurance coverage provided by MEARIE for commercial and general liability and auto actually declined 6.2% from 2008.

LPMA submits that it is appropriate for the Board to use the actual figure for 2009 insurance costs rather than the forecast because this information is available. Unlike most OM&A costs, insurance premiums are usually known before the start of the year to which they apply.

iii) Celebration Expenses

London Hydro proposes to include $30,000 for a special celebration marking London Hydro's 100th anniversary in its advertising expense to be recovered from ratepayers (Exhibit 4, page 28).

In the response to LPMA Interrogatory #36, London Hydro indicates it intends to spend this money to educate their customers about the history behind the operation of London's electric utility, from the early stages of Sir Adam Beck, to today, and beyond.

The interrogatory response then goes on to say that this celebration will also be used to continue to educate customers about living safely with electricity and to communicate ways to reduce energy consumption.

LPMA submits that London Hydro should not be allowed to recover any of the $30,000 in "celebration" expenses from its ratepayers. London Hydro has provided no evidence to support its contention that this celebration will provide additional information to ratepayers on safety or conservation over and above what London Hydro does as part of

the normal course of business. Ratepayers should not be expected to pay for a "history lesson". The shareholder of London Hydro has decided to celebrate the anniversary of the company it owns. This is properly a shareholder cost, and should not be imposed on ratepayers.

iv) Office Equipment Services & Maintenance

London Hydro has forecast a significant increase in the costs associated with office equipment services & maintenance of $294,600 or 28.6% in 2009 as compared to 2008. The main reason for this increase is the software maintenance fees associated with the new SAP customer information system that was to be completed in 2009 (Exhibit 4, page 41).

LPMA submits that London Hydro has failed to provide adequate evidence related to this significant increase in expense. No information was provided to reflect the annual software maintenance costs associated with the new customer information system.

LPMA submits that the Board should require London Hydro to provide the contracted cost for the software maintenance for 2009 in its reply Argument. If London Hydro does not provide this information, or provides a cost that is significantly lower than the $294,600 increase forecast in this category for 2009, then the Board should disallow a significant portion of the difference.

v) Corporate Training and Employee Expenses

London Hydro had forecast an increase in corporate training and employee expenses for 2008 to $813,800, from an actual level of $691,740 in 2007. The 2007 level of expenditures in this category were significantly higher than the levels recorded in previous years. These figures are shown in the response to LPMA Interrogatory #33.

As shown in the interrogatory response, actual spending in 2008 was lower than the 2007 level at $640,157. This level of spending is more than $170,000 lower than the forecast.

LPMA submits that an increase in corporate training and employee expenses from $640,157 in 2008 to $932,900 is unjustified. This is an increase of $292,743 or 45.7% over the actual 2008 figures.

In its evidence on this topic, London Hydro has provided some justification for a 14.6% increase in 2009 expenses (Exhibit 4, pages 48-50). Given the significant level of under spending in 2008 relative to the forecast of $173,643, LPMA submits that an appropriate forecast for 2009 would be attained by increasing the actual 2008 expenditures by 14.6%. This would yield a 2009 figure of $733,620, and result in a reduction in the revenue requirement for 2009 of $199,280. This level of expenditures is more in line with past historical experiences, and is still significantly higher than the level of expenditures recorded in recent years. LPMA notes that London Hydro has not provided any reasons for the significantly lower expenses in 2008 as compared to the forecast.

vi) Cost Recoveries - 1

In its original evidence, London Hydro was forecasting an increase in cost recoveries to offset OM&A costs of 1.5% or $53,000 in 2009 as compared to the 2008 forecast (Exhibit 4, page 57). As shown in the response to LPMA Interrogatory #33, the actual 2008 recoveries were nearly $120,000 higher than forecast. The implication is that now London Hydro is actually forecasting a decrease in these cost recoveries in 2009 relative to actual 2008. LPMA submits that this is not reasonable.

London Hydro was forecasting a small increase in cost recovery in 2009. LPMA submits that the cost recovery forecast for 2009 should be increased to at least the actual 2008 level. This would increase the cost recovery forecast for 2009, and reduce the corresponding revenue requirement, by $66,986. London Hydro has not provided any justification that would see a reduction in cost recovery from 2008. It is the view of LPMA that using the 2008 level is an appropriate forecast for 2009 because it is based on the most recent information available.

vii) Cost Recoveries – 2

In addition to the above, LPMA submits that London Hydro has underestimated the cost recoveries due to the increase in the available apprenticeship training tax credits. These credits are included in the cost recoveries, as indicated on page 57 of Exhibit 4.

Specifically, as shown in the response to Board Staff Interrogatory #32, the cost recoveries for 2009 included $28,000 related to the apprenticeship training tax credit. The actual calculation of this amount is shown in the response to part (d) of LPMA Interrogatory #59.

As indicated in the response to part (e) of the LPMA interrogatory noted above, the apprenticeship tax credits have now been increased to $70,000 as a result of the March Provincial budget. London Hydro has indicated in its Argument-in-Chief that it accepts this increase in the apprenticeship training tax credit. However, it does not appear that London Hydro has reflected the increase in the credits from $28,000 to $70,000 in its revised revenue requirement calculation.

LPMA submits that the cost recoveries should be increased by $42,000 to reflect the increase in the apprenticeship training tax credits as a result of the March Provincial budget.

viii) Labour & Benefits

The actual level of labour & benefits included in OM&A expenses for 2008 was $18,761,242. This expense reflects total salaries, wages & benefits, reduced by amounts allocated to capital, billable and other. These figures are shown in the revised Table 9 provided in response to LPMA interrogatory #33. This actual figure is approximately $487,000 higher than the forecast for 2008. The corresponding forecast for 2009 is $19,393,700, an increase of 3.37% from the actual 2008 level.

The increase of 3.37% in labour & benefits included in OM&A costs is made up of two components. The first of these is a 4.67% increase in total salaries, wages & benefits.

The second component is an increase of 8.78% in the allocation of costs to capital, billable and other. All of these figures are shown in the revised Table 9 attached to the response to LPMA interrogatory #33.

Base wage increases at London Hydro have been in excess of inflation over the 2004 through 2008 period. As noted above, inflation averaged less than 2.2% over this period. However, as shown in Table 10 in Exhibit 4, base wage increases have been 3.00% per year in each of 2005 through 2008. The forecast for 2009 is based on an even higher level of 3.25%. In fact, as shown in the response to LPMA Interrogatory #34, the increase in base wages for the Executive group is even higher than this at 3.90%.

LPMA submits that an increase in excess of inflation in the midst of a recession is not reasonable. The table shown in Appendix A to this argument shows the calculation of the base wages if an inflation rate of 2.3% is applied to the actual 2008 average base wage per employee. The actual 2008 average base wage per employee is shown in Table 17 in the response to School Energy Coalition Interrogatory #7. The inflation rate of 2.3% is the inflation rate used by the Board in the calculation of the 2009 price cap for the IRM plans.

As shown in Appendix A to this Argument, the application of the inflation rate of 2.3% to the actual base wage per employee for 2008 results in cost increases in some employee categories in 2009 and decreases in others. Overall the total base labour cost forecast decreases by $174,808 from that forecast by London Hydro. Allocating 25% of this figure to capital, billable and other results in the remaining $131,106 as a reduction in the labour & benefit costs in OM&A. The 25% figure is based on the response to LPMA Interrogatory #33. In the revised Table 9 included in that response, the allocation to capital, billable and other is 25% of the total salaries, wages and benefits.

LPMA therefore submits that there should be a reduction in labour & benefits in OM&A included in the revenue requirement of $131,106, based on the analysis provided above.

LPMA notes that it is not proposing any changes to the costs associated with premium pays or benefit costs.

ix) Summary

In summary, LPMA submits that a reasonable decrease in the OM&A expense forecast for 2009 is in the range of $500,000 to $600,000. The above analysis provides a reduction of $501,112. This figure is summarized in the following table.

Category of Expense	Amount ($)
2009 Rate Rebasing Costs	17,637
Insurance Costs	56,103
Celebration Expenses	30,000
Corporate Training & Employee Expenses	199,280
Cost Recoveries - 1	66,986
Cost Recoveries – 2	48,000
Labour & Benefits	131,106
Total (1)	549,112

(1) Total excludes any reduction related to Office Equipment Services & Maintenance

Reducing the OM&A forecast from $28,169,400 by this amount of $549,112 produces a 2009 forecast cost of $27,620,288. This still provides a healthy increase in OM&A expenses for London Hydro of nearly $1.24 million or about 4.7% over the actual 2008 expense level. LPMA submits that this increase, while still large, is more in line with the current economic circumstances. It is also in line with the 4.8% increase in actual OM&A expenses recorded in 2008 relative to 2007.

LPMA notes that the proposed reduction of $549,112 as proposed above is similar to reductions that would be expected under an "envelope" approach using the two following comparisons.

First, as shown in the response to LPMA Interrogatory #52, a 4.8% increase over the actual 2008 actual OM&A expenses would result in a reduction in the revenue requirement of $524,532.

Second, as shown in the response to LPMA Interrogatory #47, application of the inflation rate of 2.3% to all OM&A costs, excluding wages and benefits, would result in the revenue requirement being reduced by $563,329.

CHARITABLE DONATIONS

As shown in the response to LPMA Interrogatory #31, London Hydro had actual charitable donations in the amount of $100,000 in 2008. The forecast for 2009 is $50,000.

In response to LPMA Interrogatory #50, London Hydro calculated the amount of charitable donations based on the recommendations of the EB-2008-0150 Report of the Board that indicates that 0.12% of the Board approved distribution revenue requirement should be allocated to low-income energy assistance programs. The amount calculated is $76,930.

LPMA submits that the Board should direct London Hydro to increase its charitable donations to the 0.12% set out in the EB-2008-0150 Report of the Board. The figure provided by London Hydro of $76,930 is a ballpark estimate since the requested distribution revenue requirement is likely to be changed as a result of the Board's Decision in this proceeding. In any event, LPMA submits that charitable donations of approximately $75,000 should be included in the approved revenue requirement.

DEPRECIATION & AMORTIZATION

LPMA has reviewed the methodology used by London Hydro to calculate the depreciation expense. This methodology is described in detail in the response to LPMA Interrogatory #39. LPMA has also reviewed the depreciation expense forecast for 2009 relative to the gross fixed assets as shown in Table 16 of Exhibit 2. Based on the average of the opening and closing fixed asset balances for 2009 the overall average depreciation rate is approximately 4.6%. This rate may appear to be a little high given that the vast majority of distributor assets are depreciated at a rate of 4.0%. However, London Hydro does have a significant addition to computer software in 2009 which is depreciated at a

rate of 20.0%. As a result LPMA submits that the overall depreciation expense as calculated by London Hydro is reasonable.

TAXES

LPMA submits that London Hydro should calculate its income and capital taxes using the most recent information available, including tax rates that are expected to be applicable to 2009. This would include any changes that have resulted from the recent federal budget. It would also include any other changes as the result of the recent provincial budget.

a) Capital Tax

LPMA accepts the calculation of the capital tax as shown in Table 37 of Exhibit 4. London Hydro has correctly applied the $15 million exemption to its rate base and has used the proper tax rate of 0.225% for the calculation.

LPMA submits that any changes in capital expenditures and/or cost of power and OM&A costs as determined by the Board should be reflected in the calculation of the capital tax since these changes will have an impact on the rate base calculation.

b) Income Tax

i) Tax Rates

London Hydro used a total tax rate of 33.0% in the calculation of income taxes in 2009 (Exhibit 4, Table 37). This rate includes a federal tax rate of 19.00% and a provincial tax rate of 14.00%. LPMA agrees that these are the appropriate tax rates to be used.

ii) Apprenticeship Training Tax Credit

In the original income tax calculation shown in Table 37 of Exhibit 4, London Hydro had forecast an amount of $17,000 for the apprenticeship training tax credit. This amount was correctly added to accounting income in the line labeled Ontario Specified Tax Credits. However, the tax credit of $17,000 was not included as a deduction on the Tax Credits (SRED) line.

In the response to LPMA Interrogatory #59c, London Hydro acknowledged that an omission was made in that the 2009 apprenticeship training tax credit was not deducted from the total calculated PILS before gross up. As part of the revised tables attached to its Argument-in-Chief, London Hydro has corrected this oversight.

In addition to properly including the apprenticeship training tax credit, London Hydro has also revised the level of the credit to reflect the increase available as a result of the March Provincial budget (LPMA Interrogatory #59d) from $17,000 to $70,000. LPMA accepts this calculation, subject to the submissions in the following paragraph. LPMA believes that the increase in the apprenticeship training tax credits have been properly reflected in the revised Table 37 Tax Calculations attached to London Hydro's Argument-in-Chief.

LPMA does have one concern with the calculation of the $70,000 in apprenticeship training tax credits as shown in LPMA Interrogatory $59. This concern is based on the number of apprentices shown for addition in 2009. In particular, there are three existing apprentice positions shown, along with four new positions in the calculation of the total credit. However, as indicated at lines 8 through 11 on page 11 of Exhibit 4, London Hydro's evidence indicates that since 2007 it has hired 4 overhead line apprentices and the 2009 plan calls for 6 additional apprentices. In the response to Board Staff Interrogatory #28, London Hydro indicates that there will be a total of 16 employees in 2009 being trained as an apprentice or learner, including 10 new additional positions for apprentices. At an average cost of $5,000 per employee, the training expenses associated with these employees included in the revenue requirement is $80,000.

LPMA invites London Hydro to provide an explanation of the different figures for the number of apprentices employed in 2009 in its Reply Argument. Seven apprentices are included in the tax credit calculation, 10 are identified in the original evidence, and up to 16 have been identified as having training costs associated with them in the Board Staff interrogatory. LPMA submits that in the absence of an explanation from London Hydro for the different numbers, only one number should be used for the tax credit calculation and the employee training costs and wages and salaries and benefits.

iii) Class 10 Asset Corrections

London Hydro has changed the CCA calculation based on the response to LPMA Interrogatory #43 and errors included in that response, as indicated in its Argument-in-Chief at paragraphs 38 and 39. London Hydro has included a revised CCA Continuity Schedule for both 2008 and 2009 as part of its Argument-in-Chief.

These changes result from the reassignment of some assets from Class 10 to Classes 8 and 50 in 2008 and 2009. The net impact on the CCA is a reduction in the deduction available in 2009 by approximately $12,000. LPMA submits that this change is appropriate and should be accepted by the Board.

iv) CCA Normalization – Software

London Hydro is proposing to normalize the CCA deduction available in 2009 to "normalize" the tax write-offs associated with non-recurring software costs totaling $6,739,874 (Exhibit 4, pages 79-80).

As a Class 12 asset, this expenditure would be deducted from taxable income in the amounts of $3,369,937 in both 2009 and 2010. There would be no further deductions available in 2011 and 2012. According to London Hydro this would mean that in 2011 and 2012 the revenues would be less than that required to cover off the PILS expense since this significant deduction would no longer be available.

London Hydro proposes to "normalize" the tax deduction associated with this non-recurring software investment over the four year period 2009 through 2011. This would result in a deduction from taxable income of $1,684,969 in 2009, one-half of the amount that is available to London Hydro on an actual basis. This reduction in the CCA is shown in the 2009 CCA Continuity Schedule as a separate line item for Class 12 Computer Software - CCA Normalization adjustment for cal of regulatory PILS.

The impact of this "normalization" is to increase the 2009 revenue requirement by $829,910 (LPMA Interrogatory #42b). LPMA submits that this is a significant impact on

the base revenue requirement which is approximately $60 million. In fact, based on the information provided in the Adjusted Application column of the revised calculation of the 2009 revenue deficiency (Exhibit 1 – Table 4) attached to the Argument-in-Chief, this increase in the revenue requirement represents nearly 11% of the claimed revenue deficiency of $7,674,877.

LPMA submits that the Board should reject this normalization request. London Hydro has presented no examples of the Board allowing the normalization of CCA deductions for PILS purposes for any other utility in Ontario (LPMA Interrogatory #42a).

London Hydro has presented no evidence to support its claim that the $6,739,874 are, in fact, non-recurring investments. These investments are related to the new SAP CIS billing system (Exhibit 4, page 79). LPMA submits that there may well be additional expenditures in the next few years related to this billing system to adapt it to changing requirements.

Further, London Hydro has presented no evidence that there will not be other non-recurring investments in the 2010, 2011 or 2012. There well may be further investments in software, or a distribution station over this period. The CCA deduction associated with these investments would help reduce the PILS payable.

Finally, London Hydro has selectively proposed to "normalize" the CCA deduction for software, despite the fact that there are other significant tax changes expected in 2010 through 2012 as compared to 2009. These changes are discussed in LPMA Interrogatory #55.

As the response to this interrogatory demonstrates, if the capital tax elimination that is scheduled to take place on July 1, 2010 were to be normalized, the 2009 base revenue requirement would be reduced by $315,190. Similarly, if the corporate tax rate reductions scheduled to be implemented over the 2010 through 2012 period, including the change in the small business tax rate reduction were to be normalized, the reduction

in the 2009 revenue requirement would be a further $578,845. In total these two reductions in the revenue requirement total just under $900,000, more than the increase in the revenue requirement that results from the London Hydro "normalization" proposal.

In the response to LPMA Interrogatory #55, London Hydro indicates that the Board's 3GIRM rate model will be used for the 2010 and subsequent rate applications and that this will allow for any adjustments that may be required due to changes in the tax rates that may not be reflected in the 2009 rate submission. This assertion is only half true since one half of the change in the revenue requirement that results from changes in tax rates is passed on to rate payers. This sharing is clearly articulated in the September 17, 2008 EB-2007-0673 *Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors.*

LPMA submits that it would not be fair to rate payers to allow London Hydro to artificially inflate the revenue requirement for 2009 through the proposed "normalization" of the software CCA under the guise that it may result in revenue shortfalls in 2011 and 2012 (without any supporting evidence) while at the same time limiting the rate payers share of tax reductions to 50% of the actual savings in those years.

LPMA submits that the Board should direct London Hydro to calculate its 2009 revenue requirement under the assumption that the maximum CCA deduction is taken for the year. This would eliminate the "normalization" proposal. LPMA notes that if the total CCA deduction available in 2011 is significantly lower than in 2009, London Hydro is free to ask for a Z factor adjustment to take this reduction into account if it exceeds the materiality threshold set by the Board.

iv) Update to Regulatory Taxable Income

LPMA submits that if the regulatory taxable income is changed as a result of the Board's Decision then the income tax calculation should also be updated to reflect the revised level of regulatory taxable income.

LOSS ADJUSTMENT FACTOR

London Hydro provided the corrected calculation of the distribution supply facility and total loss factors in the response to Board Staff Interrogatory #38. This correction changed the total loss factor from 3.68% to 4.11%. The 4.11% figure is the sum of a three year average for the supply facility loss factor of 0.44% and a five year average distribution loss adjustment factor of 3.67% and was based on historical data from 2003 through 2007.

The reason for using a three year average for the supply facility loss factor was due to the abnormal 2004 results as shown in the corrected Table 35 included in the response to Board Staff Interrogatory #38. However, a review of the supply facility loss factor for 2004 reveals that it is not abnormal in relation to the other years provided. LPMA assumes that the reference to the abnormal 2004 results should have been to the abnormal 2003 results. However, LPMA does not believe that the 2003 results are abnormal either.

In any event, LPMA submits that the Board should determine the loss adjustment factor based on the most recent information available and based on a three year average for both the supply facility loss factor and the total distribution loss factor. As shown in the response to LPMA Interrogatory #41, the total loss factor would be 3.93% based on the last three years of actual data, 2006 through 2008. LPMA submits that this total loss factor, and the corresponding 0.41% supply facility loss factor and 3.53% distribution system loss factor are the appropriate factors to be used.

REVENUES

a) Forecast Methodology

i) A Flawed Methodology

London Hydro uses a combination of a top down and a bottom up approach to preparing a forecast of volumes by rate class. The top down methodology involves the use of an econometric model to forecast total system purchases. This forecast is a normalized forecast. LPMA has a number of submissions on the econometric equation used in this top down approach in section (ii) below. LPMA also has a number of adjustments that it

believes should be made to arrive at the total energy billing forecast. These suggested adjustments are detailed in part (b) below.

The bottom up approach takes a projection of the number of customers by rate class and multiplies it by a projection of the average use by rate class to arrive at a non-normalized volume forecast. The weather sensitive rate classes (or portions thereof) are then adjusted so that the total bottom up forecast by rate class in aggregate equals the normalized total energy billing forecast from the top down approach.

LPMA has a number of concerns with this approach. Suggestions for future forecast methodologies are presented in section (iii) below.

The major concerns with this methodology that forces the rate class non-normalized forecasts to add up to the normalized total energy billing forecast are summarized below.

- The weather adjustment shown in Table 18 of Exhibit 3 is done to force the sum of the non-normalized forecasts to add up to the normalized total energy billing forecast that is derived through the use of the econometric equation. There are two flaws with the methodology used. The first flaw assumes that the weather adjustment is proportional to the weather sensitive kWh forecast for each of the rate classes. For example, based on the percentages in Table 16 applied to the volumes in Table 18, the residential class has 42.4% of the weather sensitive energy, so the weather adjustment assigned to the residential class is 42.4% of the total adjustment needed to bring the two forecasts into agreement (i.e. 154 GWh). There is no reason to expect that residential customers have the same level of sensitivity to the weather as do GS < 50 kW or GS > 50 kW. Indeed, it would be expected that all four classes have different levels of sensitivity to the weather. It should be noted that in the revised Table 18 provided in the response to VECC Interrogatory #41, the Large Use and Co-Generation rate classes also have some level of weather sensitivity associated with them.

- Second, the use of non-normalized average use forecasts for the weather sensitive accounts will bias the forecast because the impact of weather on average use is different by rate class. A change of one degree day or heating degree days cannot be expected to have the same proportional impact on the average use of the weather sensitive customer classes. This bias can be seen by looking at the forecasts proposed by London Hydro for the residential and GS < 50 kW classes. London Hydro proposes to use a forecast of annual kWh usage per customer that is based on the growth rates in use over the 2000

through 2007 period, as shown in Table 13 of Exhibit 3. The average use for the GS < 50 kW class increased on average by 1.32% over this period; residential use decreased on average by 0.04%; the GS > 50 kW average use rose by 4.26%. Yet all of these customer classes experienced the same weather conditions over this period. This illustrates that historically, the impact of weather on these four classes of customers is quite different from one another.

- If there is change in the average use for a class from that originally forecast, this change does not have an impact on the total energy billing forecast using the London Hydro methodology. This is a perverse result. An increase in the average use per customer in one of the rate classes increases the weather normalized billed energy forecast in 2009 for that rate class. However, because the total weather normalized billed energy forecast for all rate classes in aggregate does not change under the forecasting methodology employed by London Hydro, the volumes for other classes must decline. Since the number of customers for these rate classes is unchanged, the underlying increase in the average use of one rate class results in an decrease in the normalized average use for each of the other customer groups. The impact of an increase in residential normalized average use results in lower volumes for streetlights, sentinel lights, unmetered loads, etc. This is not a logical result.

  A similar illogical result happens when the number of customers is changed, as shown in the response to LPMA Interrogatory #19. This interrogatory asked for the impact on the forecast if there were 150 more GS < 50 kW customers in 2009 than that forecast by London Hydro. The net impact can be seen by comparing Table 22 in the interrogatory response to the original Table 22 in Exhibit 3 at page 23. At the bottom of the table the total customers/connections kWh and kW from applicable classes is shown. Comparing these two tables reveals the following: the number of customers/connections by 150 to 182,539, the total **kWh remains unchanged** and the kW from applicable classes **declines** by 5,200 to 4,608,732! Only the first of these three results make sense. There is no rationale for no increase in total kWh. There is even less rationale for a decrease in kW for the rate classes that use this as a billing determinant (which of course, does not include the additional 150 customers in the GS < 50 kW customers).

  A review of Table 6 in the interrogatory response and that provided in the original evidence provides even more startling results. The impact of adding 150 GS < 50 kW customers results in a reduction in the normalized average use per customer in not only the GS < 50 kW rate class, but also in the residential and GS > 50 kW class! Apparently the secret behind successful CDM in the residential sector is increasing the number of general service customers!

- The econometric equation used to forecast the total system purchases cannot adequately and/or accurately reflect the relevant drivers when these drivers are different for different rate classes. Further details are provided in the following section.

ii) Econometric Equation

The econometric equation used to forecast the total system purchases suffers from a number of deficiencies. Each of these deficiencies is noted below.

- By aggregating all volumes into a single equation, the methodology assumes that all rate classes are affected by the same drivers such as heating degree days, cooling degree days and real GDP. There is not evidence to support that this is the case.

- By aggregating all volumes into a single equation, the methodology assumes that all rate classes are affected to the same degree for each driver included. It is unlikely that the weather, for example, has the same impact on residential customers as it does on large general service customers. Similarly, general service volumes are likely to be more influenced by changes in real GDP than are residential volumes.

- The equation does not have any explicit relationship to the number of customers. It is in effect, independent of the number of customers. It is not reasonable to expect that the total purchases are not driven at least in part by the number of new customer additions.

- The equation implicitly assumes that the impact of weather (heating and cooling degree days) has the same impact across all months (or seasons) of a year. For example, 1 additional heating degree day in January has the same impact on total system purchases as one additional heating degree day in July. It is extremely doubtful that this is true. The impact of weather will be different by month.

- The model used does not include any type of variable to model conservation. The inclusion of a simple trend variable may capture both conservation (including naturally occurring conservation) and other trends in the use of electric appliances.

LPMA submits that these are just some the major deficiencies of the current econometric equation and the forecast that results from its use. In the following section, suggestions are provided for improvements in the forecast methodology, including using a bottom up regression analysis by rate class that would eliminate or minimize most of the deficiencies noted above.

iii) Future Forecasts

LPMA recommends that the Board direct London Hydro to develop a forecasting methodology that generates a forecast of billed energy on a bottom up basis. In other words, a forecast is developed for each rate class and these forecasts add up to the overall forecast, rather than the top down approach used by London Hydro in this application.

The forecast for each rate class would be based on a forecast for the number of customers in each rate class and a forecast of normalized average use for each rate class. The latter would be based on an econometric estimation of average use based on a number of explanatory variables that could differ by rate class. The forecast of customers could be driven by economic activity and/or local developments.

Such a process would enable London Hydro to distinguish between the drivers of volumes by rate class. The current methodology groups all volumes together and attempts to determine what the drivers are of the total. LPMA submits that this approach loses much of its explanatory power because different rate classes are driven by different factors and to different degrees by the same factor. As noted earlier, the impact of weather on residential customers is likely to be different than the impact on large general service customers. The current methodology attempts to "average" these impacts across all customer classes.

b) Adjustments to the Forecast

London Hydro, in the response to VECC Interrogatory #15d, indicated that it had failed to take into account the weather sensitivity for some rate classes in its original forecast. Further, in response to VECC Interrogatory #41a, London Hydro confirmed that it proposed to update the 2009 load forecast to reflect the corrected values when final rates for the draft rate order are determined. London Hydro has quantified the impact of this change in paragraph 28 of its Argument-in-Chief to be an increase in revenues at existing rates of $68,525. LPMA submits that the Board should accept this increase as it is the direct result of the correction of an oversight in the original evidence.

c) Other Distribution Revenue

London Hydro originally forecast other distribution revenues to total $3,707,148 in the test year. As a result of the interrogatory process, London Hydro has made a number of corrections and adjustments to this figure. These adjustments are summarized in paragraph 20 of London Hydro's Argument-in-Chief and are shown in the revised Exhibit 3, Table 23 immediately following that paragraph. The net impact is a small reduction in other distribution revenues to $3,694,100. LPMA accepts these changes as being appropriate.

As shown in the response to LPMA Interrogatory #21, the actual level of other distribution revenues recorded in 2008 was $3,991,704. As a result the 2009 forecast of $3,694,100 represents a significant drop in these revenues of nearly $300,000 or 7.5%.

The largest contributing factor to this decline is a reduction of nearly $200,000 related to office space that previously rented to the City of London (Exhibit 3, page 27). The other main source of the overall decline is a reduction in interest and dividend income. LPMA accepts the overall reduction in other distribution revenues as being reasonable.

DEFERRAL AND VARIANCE ACCOUNTS

London Hydro is proposing to clear the account balances to rate payers for four accounts as part of this proceeding. These accounts are 1508 –Other Regulatory Assets – Sub-account OEB Cost Assessments, 1508 – Other Regulatory Assets – Sub-account Pension Contributions, 1525 – Miscellaneous Deferred Debits, and 1580 Retail Settlement Variance Account – Wholesale Market Service Charges.

The disposition of this last account (1580) has usually been deferred by the Board as it expects to deal with this account as part of a generic review of the disposition of commodity accounts. However, London Hydro notes that Toronto Hydro and Horizon were allowed to dispose of the balances in this account. London Hydro proposes to include this account in its disposition as part of this proceeding to offset the rate increases that would result from the disposition of the other three accounts.

London Hydro indicates in its evidence (Exhibit 5, page 2) that it would be inappropriate for it to seek recovery of the three accounts with debit balances from customers without requesting approval from the OEB to return the significant credit balances owing to rate payers in account 1580. LPMA agrees with this rationale.

LPMA notes that there appears to be a debit balance in the remaining deferral and variance accounts that London Hydro has NOT submitted for recovery or clearance with this application (Exhibit 5, Table 1) of approximately $1.5 million. This compares to the net rebate to customers of approximately $4.3 million shown in Table 2 of Exhibit 5 that London Hydro is proposing to give back to customers as part of this application.

LPMA has also reviewed the submissions of Board Staff related to the disposition of deferral and variance accounts. Staff submits that it should consider altering the London Hydro proposal to include the disposition of all the account balances shown on lines 1 through 11 in the table on pages 36-37 of the Staff Submission dated June 24, 2009.

LPMA would not be opposed to the Board directing London Hydro to dispose of more of the debits in the remaining accounts as part of this proceeding. This would reduce the rebate to customers from that proposed by London Hydro, but it would reduce the amount to be collected from them in the future. The benefit of this approach would be less variability in rates over time due to the clearance of these additional accounts as proposed by Board Staff.

LPMA submits that whichever balances are ultimately recovered/rebated from customers, the rate rider should be calculated over the period from the implementation date of the decision in this application through April, 2011.

LPMA notes the Board Staff submission in the Low Voltage Costs section in relation to account 1550 – Low Voltage and supports the Staff submission that this account should be cleared and closed.

LRAM AND SSM

London Hydro is not requesting the recovery of any lost revenue or shared savings as part of its application (Argument-in-Chief, page 34 & LPMA Interrogatory #46). London Hydro indicates that this means it has forgone approximately $617,000 in lost revenue related to CDM. This decision has been made to help minimize the impact on rate payers. LPMA notes that the figure of $617,000 has not been tested in this proceeding, but supports the proposal of London Hydro to forego the lost revenue amount.

London Hydro has also indicated that it is not seeking to recover the costs associated with its Earth Day 2007 campaign (LPMA Interrogatory #2). LPMA also supports this proposal from London Hydro.

COST OF CAPITAL

a) Capital Structure

London Hydro is requesting a deemed equity component of 40.0, short term debt of 4.00% and long term debt of 56.0% (Exhibit 6, Table 1). LPMA accepts this capital structure as it is in compliance with the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006.

b) Return on Equity

London Hydro had requested a return on equity of 8.57% in the test year (Exhibit 6, page 3). In the response to LPMA Interrogatory #30a, London Hydro acknowledged that this rate would be updated by the Board and that this data was released on February 24, 2009. The data indicated that the return on equity would be 8.01%.

In its' Argument-in-Chief, London Hydro has confirmed that it has adjusted its application to reflect a requested return on equity of 8.01% (pages 19-21). LPMA accepts this adjustment as it is compliance with the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006.

c) Short Term Debt Rate

London Hydro had requested a short term debt rate of 4.47% in the test year (Exhibit 6, Table 2). In the response to LPMA Interrogatory #30a, London Hydro acknowledged that this rate would be updated by the Board and that this data was released on February 24, 2009. The data indicated that the short term debt rate would be 1.33%.

In its' Argument-in-Chief, London Hydro has confirmed that it has adjusted its application to reflect a requested short term debt rate of 1.33% (pages 19-21). LPMA accepts this adjustment as it is compliance with the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006.

d) Long Term Debt Rate

LPMA submits that there are two issues that need to be dealt with under the heading of the long term debt rate. These issues are the rate to be applied to the embedded affiliate debt and the rate to be applied to the unfunded long term debt. London Hydro has a deemed amount of long term debt of approximately $126 million (Exhibit 6, Table 1), of which $70 million is an unsecured promissory note from an affiliate. The remaining $56 million is notional, or deemed long term debt.

i) Embedded Affiliate Debt

London Hydro has an unsecured promissory note held by the Public Utilities Commission of the City of London in the amount of $70 million (Exhibit 6, page 1). This debt is both affiliate debt (Exhibit 6, page 2) and, in the view of London Hydro, callable debt (Exhibit 6, page 3). This debt instrument bears an interest rate of 6.0%.

London Hydro indicates in its Argument-in-Chief that it is *"conscious of the importance of minimizing impacts on its rate payers, particularly in light of current economic circumstances"* (Argument-in-chief, page 6). The Argument-in-Chief then goes on to list a number of the rate mitigation measures that London Hydro has used in this application.

At paragraph 14 of the Argument-in-Chief, London Hydro indicates that the $70 million in affiliate debt is callable on demand and that based on other Decisions and the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006, this debt would attract the Board's deemed rate of 7.62%. However, London Hydro goes on to state that it is requesting a rate of only 6.0% on the $70 million note. This is the existing rate on this debt instrument. London Hydro calculates the forgone revenue to be $1,134,000.

LPMA submits, however, that London Hydro is not entitled, in any event, to request use of the deemed long term debt rate on this embedded debt. The *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006 states that for all variable rate date and all affiliate debt that is callable on demand the deemed long term debt rate should be used. The evidence indicates that the rate on this long term debt is fixed at 6.0%, hence it is not a variable rate debt. The question then becomes whether or not it is callable on demand.

The evidence indicates that this note is callable on demand with 367 days notice. The evidence also indicates that the note has a fixed term, maturing on October 31, 2010. There is no evidence on the record that the note has been called. With 367 days notice required, the note now cannot be payable during the 2009 test year. LPMA submits that based on this evidence the note cannot and should not be considered callable.

The *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006 also states that for embedded debt the rate approved in prior Board decisions shall be maintained for the life of each active instrument, unless a new rate is negotiated, in which case it will be treated as new debt. LPMA submits that this note is embedded debt at a fixed rate of 6.0%. This rate was approved in London Hydro's EB-2005-0389 rates proceeding for 2006 rates. Since that time, no new rate has been negotiated. The only change to the note is that the life has been extended to the earlier of 367 days after demand or October 31, 2010. As of the

end of 2008, the note has not been called. As a result, this debt will not have to paid off in the current 2009 test year.

LPMA submits that the Board should accept the 6.0% rate on this debt as requested by London Hydro. It does not have to paid off during the test year. As a result, London Hydro will not be required to go to the market and try and replace it, at a potentially higher rate during the test year. Rate payers should be expected to pay only for the cost of debt that will be incurred during the test year.

ii) Unfunded Long Term Debt

Unfortunately, LPMA cannot support London Hydro's request to use the deemed long term debt rate applied to the deemed, or unfunded long term debt of approximately $56 million.

London Hydro states in the response to LPMA Interrogatory #30b that it *"would expect that the Board will allow the deemed rate of 7.62% to apply to this portion of London Hydro's deemed long-term debt"*.

In the response to Board Staff Interrogatory #109, London Hydro provides its rationale for its request. This rationale is based on the Hydro One Remote Communities Inc.'s 2009 Decision and on the Decision and Order for COLLUS Power Corp.'s 2009 rates. In its' Argument-in-Chief, London Hydro also relies on the EB-200800233 Decision for Innisfil Hydro. LPMA deals with each of these Decisions in turn.

The Hydro One Remote Communities Inc. (EB-2008-0232) Decision states at page 12:

> *"The Board finds that it is not appropriate to apply the Board's deemed long-term debt rate to the notional or deemed long-term debt. The two are quite separate concepts. The deemed long-term debt rate is intended to apply in the absence of an appropriate market determined cost of debt, such as affiliate and variable rate debt situations. For companies with embedded debt, it is the cost of this embedded debt which should be applied to any additional notional (or deemed) debt that is required to balance the capital structure."*

London Hydro emphasizes the third sentence in this paragraph to justify their position. In particular, London Hydro appears to interpret this sentence to mean that the deemed long-term debt rate is intended to apply in the absence of an appropriate market determined cost of debt, including third party debt. LPMA submits that this is an incorrect interpretation of the Board's deemed long term debt rate.

In the *Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario Electricity Distributors* dated December 20, 2006 the Board clearly states that the deemed long-term debt rate will be used for two purposes. First, for new affiliated debt, the Board determined that the allowed rate would be the lower of the contracted rate and deemed long-term debt rate. Unfunded debt is neither new debt nor affiliated debt. The second use of the deemed long term debt rate is for all variable-rate debt and for all affiliate debt that is callable on demand. Again, unfunded debt is neither variable-rate nor is it callable affiliate debt. In the response to Board Staff Interrogatory #109 London Hydro correctly defines unfunded long term debt as the portion of its deemed debt for which no actual debt exists. It is clear to LPMA that the deemed long term debt rate does not apply to deemed (unfunded) debt.

In the Hydro One Remotes Decision noted above, the Board explicitly said that it is not appropriate to apply the Board's deemed long term debt rate to the notional or deemed long term debt. Notional or deemed long term debt has the same meaning as unfunded debt. The Decision then goes on to state that the cost of the embedded debt is that which should be applied to any additional notional (or deemed) debt that is required to balance the capital structure.

LPMA notes that the Board came to the same conclusion in its Decision with Reasons dated May 28, 2009 in EB-2008-0272 which was an application by Hydro One Networks Inc. for transmission revenue requirement and rates for 2009 and 2010. In that Decision the Board stated:

> *"The Board agrees with intervenors that it is not appropriate to apply the Board's deemed long-term debt rate to the notional or deemed long-term debt. The two are quite separate concepts. The deemed long-term debt rate is clearly intended to apply*

in the absence of an appropriate market determined cost of debt, such as affiliate and variable rate debt situations. For companies with embedded debt, it is the cost of this embedded debt which should be applied to any additional notional (or deemed) debt that is required to match the capital structure to the Board's deemed capital structure. This is consistent with the treatment given to LDCs that have undergone rebasing in 2008 and 2009".

In the response to Board Staff Interrogatory #109b, London Hydro makes reference to the Decision and Order of the Board in EB-2008-0226 for COLLUS Power Corp. The section of the Decision that London Hydro says supports its positions is reproduced below:

> *"The Board finds that this rate* (the Board's current deemed long term debt rate of 7.62%) *will also be applicable to COLLUS' promissory not as it is callable affiliate debt".*

LPMA submits that this does not support London Hydro's position, as the application of the Board long term debt rate is clearly related to callable affiliate debt, not unfunded debt.

In its Argument-in-Chief, at paragraph 50, London Hydro uses the examples of the Innisfil Hydro (EB-2008-0233) and COLLUS (EB-2008-0226) Decisions as support for its conclusion that it should be allowed to recover 7.62% on the portion of the deemed long term debt that is classified as unfunded as being *"consistent with the Decisions of the Board for other 2009 rebasing applicants that only have affiliate debt that is callable on demand."*

LPMA submits that this is factually incorrect. Innisfil Hydro's evidence is quite clear that they had third party debt in addition to affiliate debt. Similarly, the evidence of COLLUS was there a significant portion of their long term debt was going to be held by a third party.

The impact on ratepayers of London Hydro seeking to use the Board's deemed long term debt rate on unfunded or notional debt of $56 million is significant. As shown in the response to LPMA Interrogatory #49c, the impact of using the deemed long term debt

rate of 7.62% in place of the embedded rate of 6.0% is an increase of $908,349 in the revenue requirement. This eliminates 80% of the foregone revenue associated with the interest rate on the embedded debt that London Hydro has proposed in order to mitigate rate impacts on rate payers. LPMA submits that it does not make sense to reduce interest costs on the one hand to help mitigate rate increases and then turn around and increase rates on a cost for debt that does not actually exist.

iii)Summary

LPMA submits that the Board should approve a long term debt rate of 6.0% on the existing embedded debt of $70 million, as requested by London Hydro. Despite the fact that this debt is eligible for the application of the Board's deemed long term interest rate, London Hydro's proposal should be accepted as a rate mitigation proposal. This will have no adverse effect on London Hydro since the rate they pay to their debt holder is the 6.0% that they are requesting that the Board approve.

The Board should also approve the application of the 6.0% embedded debt rate to the unfunded debt of $56 million. This is consistent with other Board Decisions dealing with distributors rebasing in 2008 and 2009.

COST ALLOCATION & RATE DESIGN

London Hydro originally provided a series of revenue to cost ratios for the various rate classes in Table 1 of Exhibit 8. As a result of a number of interrogatories from Board Staff and VECC, London Hydro made additional adjustments to the data. The resulting revenue to cost ratios have been summarized by Board Staff in the table on page 28 of their Submissions. The table provided in the Staff Submissions also provides ratios for 2009 and 2010, as proposed by London Hydro.

London Hydro is proposing to adjust the revenue to cost ratios over a two year period to achieve revenue to cost ratios that fall within the OEB-approved ranges for all customer classes by the end of this two year period. In particular, London Hydro proposes to increase the revenue to cost ratios for those classes that are currently below the OEB-

approved ranges. LPMA submits that the starting point for the change should be the second column of ratios provided in the table at page 28 of the Staff Submissions. Based on this starting point, the ratios should be increased for the GS 50 – 4999 kW (71.2%), Large Use > 5 MW (62.0%), street lighting (17.3%), sentinel lighting (14.7%) and unmetered scattered load (58.3%) classes. LPMA submits that it should direct London Hydro to increase the ratio for these classes to the lower end of the OEB-approved ranges in 2009, except where the change results in rate impacts of more than 10%. For those classes, the increase should be phased in over two years. This is consistent with what London Hydro is proposing for these rate classes. However, as noted in the Staff Submissions, the ratios proposed by London Hydro are based on movement from the originally filed ratios, not the corrected values. LPMA submits that the movement should be from the corrected values. This may or may not require that the two year phase in be applied to the GS 50-4999 kW and the Large Use class as their correct ratios are lower than the original values.

Two rate classes are at revenue to cost ratios above the upper limit of the OEB-approved range – GS < 50 kW (129.2%) and GS 50-4999 kW Co-Generation (239.7%). LPMA agrees with the proposal to move the GS < 50 kW class to 120% in 2009, which is the upper end of the OEB-approved range. LPMA also agrees with the proposal to lower the ratio to the upper end of the OEB-approved range for the Co-Generation class, as proposed by London Hydro.

The two remaining rate classes (residential & standby power) are at or within the approved ranges.

London Hydro proposes to use the incremental revenue generated by moving those classes below the lower limit of their respective OEB-approved ranges to lower the residential customer class ratios in both 2009 and 2010. LPMA does not agree with this proposal.

In 2009, LPMA submits that the incremental revenue generated should first be used to bring the GS < 50 kW ratio down to 120% (as proposed by London Hydro) and to reduce the ratio for the Co-Generation class to 209.9%. This is the mid-point between the upper end of the approved range of 180% and the current correct ratio of 239.7%. Any remaining incremental revenue would then be used to reduce the residential ratio. This is generally consistent with what London Hydro has proposed.

However, in 2010, LPMA submits that the incremental revenue generated by moving the remaining distance to the lower end of the approved ranges should not all be allocated to the residential rate class. The revenue to cost ratio for the residential class, at 107% in 2009 is already well within the approved range. However, the other rate class that contains a large number of customers, GS < 50 kW, remains at 120% in 2010 under the London Hydro Proposal. LPMA submits that this is not fair to those customers because they are significantly higher above a ratio of unity than are the residential customers. LPMA submits that the Board should direct London Hydro equally split the incremental 2010 revenue between the residential and GS < 50 kW customers to reduce ratios for both classes. This is a more equitable approach than allocation the incremental revenues only to the residential class. Based on the information provided in Table 3 of Exhibit 8, the LPMA proposal would still provide a reduction in the revenue to cost ratio for the residential class of about 0.6, from 107.0% in 2009 to 106.4% in 2010. At the same time, the ratio for the GS < 50 kW class would decline from 120.0% in 2009 to about 117.5%.

COSTS

LPMA requests that it be awarded 100% of its reasonably incurred costs. Recognizing the size of London Hydro and the number of intervenors in this proceeding, LPMA has attempted to minimize its time on this application, while at the same time ensuring a thorough review.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

June 26, 2009

Randy Aiken

Consultant to LPMA

APPENDIX A TO LONDON PROPERTY MANAGEMENT ASSOCIATION ARGUMENT

	Actual 2008 Base Salary per Employee (a)	Forecast 2009 Base Salary per Employee (b)	Number of Employees (FTE) (c)	Base Compensation (d) = (b) x (c)	Forecast Base Compensation (e)	Difference (f) = (d) - (e)
Executive	166,158	169,980	5.0	849,898	851,600	(1,702)
Directors	117,379	120,079	9.0	1,080,708	1,052,900	27,808
Middle Management - Supervisory	82,363	84,257	36.0	3,033,265	3,056,100	(22,835)
Non-Union - non-supervisory	71,093	72,728	35.0	2,545,485	2,630,700	(85,215)
Union	59,673	61,045	176.0	10,744,004	10,902,500	(158,496)
Non-permanent	41,751	42,711	17.9	764,532	698,900	65,632
Total				19,017,892	19,192,700	(174,808)
Allocation to Capital, Billable and Other (g)						(43,702)
Labour & Benefits in OM&A						(131,106)

(a), (c), (e) Appendix SEC 7 - Table 17
(b) Based on inflation rate of 2.3%
(g) Based on 25% allocation factor derived from revised Table 9 in LPMA Interrogatory # 33