

## SUMMARY OF APPLICATION

Hydro One Networks Inc. (“Hydro One” or “Hydro One Distribution” or “the Company”) is applying for an Order approving the revenue requirement, cost allocation and rates for Hydro One’s Distribution Business for the year 2008 (“test year”) in accordance with the memorandum dated May 4, 2007, provided by the Ontario Energy Board (the “Board” or “OEB”), under Docket Number EB-2006-0330. This summary provides a brief description of the approvals being sought through this Application and a summary of reasons for the increase in revenue requirement.

### 1.0 SCOPE OF APPLICATION

The scope of this Application includes:

- the review of Hydro One’s evidence in support of Distribution revenue requirements for 2008,
- the review of revised Distribution rates to be implemented in 2008, and
- the review of Hydro One’s proposal for harmonizing acquired LDC and legacy customers’ distribution rates into a reduced number of new rate classes over a 4 years period.

In its December 20, 2006 Cost of Capital report under Proceeding EB-2006-0088/EB-2006-0089, the Board determined that a deemed capital structure of 60% debt and 40% common equity was appropriate for all distributors in determining their revenue requirements. Hydro One has applied the Board’s deemed capital structure of 60% debt and 40% common equity in determining its 2008 revenue requirements. For the 2008 test year, as per the Board’s formulaic approach in Appendix B of the Cost of Capital Report, Hydro One has applied an equity return of 8.64% using the May 2007 Consensus

1 Forecast. The Company assumes that when the Board reaches its decision in this  
2 Application, Hydro One will be instructed to recalculate its 2008 test year equity return  
3 using a more current 2008 Consensus Forecast.

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5 The Board's Decision on Hydro One's Distribution rates for 2006 under Proceeding RP-  
6 2005-0020/EB-2005-0378 approved methodologies to establish common corporate cost  
7 allocation, working capital and depreciation. The same methodologies were applied for  
8 and approved by the Board in their Decision on Hydro One Transmission's application  
9 under Proceeding EB-2006-0501, which included a 2008 test year. To ensure  
10 consistency is maintained for the 2008 test year, which is common to both the  
11 Distribution and Transmission Businesses, Hydro One has utilized these same  
12 methodologies. The interest rate used for construction work in progress (CWIP), also  
13 referred to as Allowance for Funds Used During Construction (AFUDC), reflects the  
14 Board's decision in EB-2006-0117, effective November 28, 2006. This decision  
15 prescribed that the interest rate to use for CWIP, effective May 1, 2006, would be the  
16 Scotia Capital All-Corporates Mid-Term Yield, as published on the Bank of Canada  
17 website and updated quarterly.

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19 Hydro One assesses the condition of its Distribution assets on an ongoing basis, and the  
20 resulting Asset Condition Assessment has been used to shape the Sustainment OM&A  
21 and Capital plans set out in Exhibits C and D. Hydro One also undertook a stakeholder  
22 consultation process to increase understanding of the issues in this Application and to  
23 provide a forum for early identification of stakeholder concerns.

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25 As discussed in Exhibit A, Tab 5, Schedule 1, this application by Hydro One Distribution  
26 is substantively consistent with the 2006 Electricity Distribution Rate Handbook ("the  
27 Handbook") issued by the Board on May 11, 2005, and with the Filing Requirements for  
28 Transmission and Distribution Applications (the "Filing Requirements") issued by the

1 Board on November 14, 2006. The evidence filed with this application is also consistent  
2 with Hydro One's Application for 2006 Distribution rates, and its Application for 2007  
3 and 2008 Transmission rates, both of which were approved by the Board.

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5 This application also fully reflects the impact of the Board's recent Decision with  
6 Reasons in EB-2007-0063, "OEB Combined Proceeding re: Smart Meters", issued on  
7 August 8, 2007. The smart meters decision is reflected and discussed in Exhibit F,  
8 Regulatory Assets.

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10 Hydro One addresses through this Application all outstanding Board directives with  
11 respect to its Distribution Business. A listing of all relevant directives and the  
12 corresponding exhibit or a statement of status is provided in Exhibit A, Tab 17,  
13 Schedule 1.

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15 In addition, over the next year, Hydro One will work within the framework of the Board  
16 established process for developing a third generation Incentive Regulation Model  
17 ("IRM"). Hydro One anticipates that it will apply the Board's third generation IRM to  
18 adjust revenue requirement components to determine annual revenue requirements in  
19 2009 and 2010.

## 20 21 **2.0 APPROVALS REQUESTED**

### 22 23 **2.1 Revenue Requirement**

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25 Respecting Hydro One's revenue requirement in the year 2008 for its Distribution  
26 Business, the Company is seeking approvals for:

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- 1 1. A revenue requirement of \$1,067 million for the 2008 test year, as set out in Exhibit  
2 E2, Tab 1, Schedule 1 on the basis of the methodology described in Exhibit E1, Tab  
3 1, Schedule 1.
- 4 2. An OM&A cost expenditure level of \$478 million in 2008 for the Distribution  
5 Business, as summarized in Exhibit C1, Tab 2, Schedule 1. Hydro One's request for  
6 this approval is supported by detailed evidence in various schedules in Exhibit C.
- 7 3. Other components of the "Cost of Service", as summarized in Exhibit C1, Tab 6,  
8 Schedule 1 and Exhibit C1, Tab 7, Schedule 1. These include Hydro One's  
9 depreciation and amortization rates and Payments in Lieu of corporate income taxes  
10 ("PILs") for the Distribution Business for 2008.
- 11 4. A Distribution business rate base of \$4,382 million in 2008 as summarized in Exhibit  
12 D1, Tab 1, Schedule 1. Hydro One's request for this approval is supported by a  
13 discussion of the assets and the capital expenditures forecast for 2008 as found in  
14 Exhibit D.
- 15 5. Regulatory assets with a total balance of \$(49) million to April 30, 2008, which  
16 would be refunded over a four-year period, as summarized in Exhibits F1, Tab 1,  
17 Schedule 1 and F1, Tab 2, Schedule 1.

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19 Approval of the revenue requirement of \$1,067 million for the 2008 test year and the  
20 regulatory assets with a total balance of \$(49) million, combined with the expiry of rate  
21 riders, established under Proceeding RP-2004-0117/0118, and expiry of smart meters  
22 interim costs, result in a net distribution rate increase of less than 2.5%, relative to 2007  
23 rates set by the OEB under the Incentive Regulation Mechanism. This distribution rate  
24 increase represents an increase of less than 1% on the average customer's total bill.

## 25 26 **2.2 Cost Allocation and Rates**

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28 With respect to cost allocation and rates, Hydro One is seeking approvals of:

- 1 1. The 2008 rate schedules including terms and conditions of service as set out in  
2 Schedule 1 of Exhibit G2, Tab 4 to Exhibit G2, Tab 94. These schedules reflect the  
3 Company's proposed Retail Transmission Service Rates and loss factors.
- 4 2. The charges for the provision of miscellaneous services as set out in Exhibit G2, Tab  
5 95, Schedule 1.
- 6 3. Hydro One Distribution's proposed cost allocation and rate design methodology, as  
7 described in Exhibit G1, Tab 1, Schedule 1 and supported by the remainder of the G  
8 Exhibit.
- 9 4. Hydro One Distribution's proposal for harmonizing acquired LDC and legacy  
10 customers' distribution rates into a reduced number of new rate classes over a 4 year  
11 period, as described in Exhibits G1, Tab 2, Schedule 5 and Exhibit G2, Tab 2,  
12 Schedule 1.
- 13 5. The modifications to the OEB cost allocation model as discussed in Exhibit G2, Tab  
14 1, Schedule 1.
- 15 6. The disposition of the balances accumulated in Regulatory Accounts as shown in  
16 Exhibit F1, Tab 2, Schedule 1.

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18 Other

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- 20 7. Hydro One also seeks approval of variance accounts to track the impact of  
21 incremental OEB costs, variances between Hydro One's planned and actual pension  
22 costs, and the deferred revenue as a result of mitigation to limit customer's total bill  
23 impacts as described in Exhibit F1, Tab 3, Schedule 1.

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1 **3.0 CAUSES OF THE INCREASE IN REVENUE REQUIREMENT**

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3 Hydro One's revenue requirement of \$1,067 million for 2008 is provided in Exhibit E2,  
4 Tab 1, Schedule 1. The main contributions to the increase in revenue requirement in  
5 2008 are:

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- 7 • Growth of about \$660 million in the installed asset base since rates were established  
8 in the year 2006. This expansion was required to install smart meters, meet growth in  
9 customer demand, replace assets damaged by storms, resolve trouble calls, and  
10 replace end-of-life assets.
  - 11 • Increases in OM&A requirements, largely precipitated by a planned increase in  
12 vegetation management, support of smart meters, lower overheads capitalized and the  
13 effects of escalation in replacement parts, materials and labour rates.
  - 14 • The increase to the Hydro One Distribution Business common equity component  
15 from 36% to 40%. This deemed capital structure was determined by the Ontario  
16 Energy Board as being appropriate for all distributors in its December 20, 2006, Cost  
17 of Capital report.

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19 These increases are offset by lower statutory tax rates, sales growth, a reduced return on  
20 equity, a decrease in asset removal costs, and lower interest rates. The increased revenue  
21 requirement combined with the expiry of rate riders, established under Proceeding RP-  
22 2004-0117/0118, and the expiry of smart meters interim costs, result in a net distribution  
23 rate increase of less than 2.5% relative to 2007 rates set by the OEB under the Incentive  
24 Regulation Mechanism, which represents an increase of less than 1% on the average  
25 customer's total bill.

1 The increases identified within the Application will ensure that customers within the  
2 Province will continue to be supplied in a secure and reliable manner, thereby  
3 contributing to the health and competitiveness of the Province's economy.

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