

Board Staff Interrogatories
2009 Incentive Regulation Mechanism Rate Application
Hydro One Networks Inc.
EB-2008-0187

Updated Application

1. Ref: Cover Letter

In the cover letter dated January 30, 2009, Hydro One Networks Inc. ("Hydro One") states that "these updates do not materially change the distribution rate proposal contained in the EB-2008-0187 application submitted by Hydro One on November 7, 2008 and outlined in the Notice of Application issued by the Board on December 10, 2008."

- a) Consistent with the methodology used to calculate the range of impacts shown in the Notice of Application, please provide a revised range of impacts on the delivery portion of the bill (\$ and %) that would arise directly from the revised application dated January 30, 2009, if approved as filed, for:
 - i) A residential customer consuming 1,000 kWh per month, and
 - ii) A small general service customer consuming 2,000 kWh per month and having a monthly demand of 50kW or lower.
- b) Please also provide a) based on total bill impacts.

Incremental Capital Investment Request

2. Ref: Exhibit B1/Tab 3/Schedule 1/Pages 1 and 2

As summarized in Table 1, Hydro One is requesting that \$174 million of its \$461 million planned capital additions in 2009 be approved as incremental capital investment, as contemplated in the *Supplemental Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors* dated September 17, 2008 (the "Supplemental Report"). This amount is the difference between the \$461 million in planned 2009 capital expenditures and the incremental capital threshold calculated on Sheet G2.1 of the 2009 3rd Gen. IRM Supplementary Filing Module (the "Sup. Module").

- a) Please confirm whether Hydro One considers the incremental capital threshold, as calculated on Sheet G2.1 of the Sup. Module, to be the appropriate demarcation between incremental and non-incremental capital, and not solely a “tool” to determine whether or not Hydro One is eligible to make an incremental capital application. If confirmed, please explain why this would be the case.
- b) On page 2, Hydro One states that “the requested revenue requirement (comprised of incremental return on rate base, depreciation and PILs associated with the incremental capital expenditures) is directly associated with the capital spending and is clearly outside of the base upon which current rates were derived. Further, these costs will not be funded by the expansion of service to include new customers or load growth.”
 - i) If Hydro One confirmed the view outlined in a), please explain how Hydro One reached the conclusion it did on page 2 and provide any analysis Hydro One prepared to support that statement.
 - ii) Please explain why the entire revenue requirement associated with the requested \$174 million in incremental capital is “clearly outside of the base upon which current rates were derived” given that the planned 2009 capital additions are only \$59 million above the 2008 re-basing year amount approved in EB-2007-0681.
 - iii) On page 3 of Exhibit B1/Tab 3/Schedule 2, Hydro One indicates that “Development capital expenditures consist of investments required to serve new customers and meet increased demand of existing customers.” Please explain why none of the incremental capital investments requested will “be funded by the expansion of service to include new customers or load growth” when the development capital, totalizing \$171 million in 2009, is comprised of capital expenditures supporting the service of new customers and load growth.
- c) Please indicate the amount of planned 2009 capital investments that is expected to qualify under the capital cost allowance (“CCA”) Class 50 and be eligible for the accelerated CCA rate announced in the January 27, 2009, federal budget. Please also indicate what the expected total tax savings will be.
- d) Please provide an indication whether expenditure levels could result in a further incremental capital request application before the end of the incentive regulation term.
- e) Please indicate when Hydro One plans on filing its next Cost of Service application.
- f) Please provide Hydro One’s capital expenditure plan for 2010.

- g) Please provide Hydro One's capitalization policy. This should include a description of the direct overhead and indirect overhead capitalized. Please provide a five-year history of the percentage of overhead capitalized in capital expenditure projects and the reasons for the choices made.

3. Ref: Exhibit B1/Tab 3/Schedule 2/Page 2

In its Supplemental Report, the Board stated on page 30 and 31 that:

"The distributors, on the other hand, perceive the module as a special feature of the 3rd Generation IR architecture which would enable them to adjust rates on an on-going, as-needed basis to accommodate increases in rate base. In the Board's view, the distributors' view is not aligned with the comprehensive price cap form of IR which has been espoused by the Board in its July 14, 2008 Report. The distributors' concept better fits a 'targeted OM&A' or 'hybrid' form of IR. This alternative IR form was discussed extensively in earlier consultations but was not adopted by the Board."

The Board further stated that, "Rather, the capital module is intended to be reserved for unusual circumstances that are not captured as a Z-factor and where the distributor has no other options for meeting its capital requirements within the context of its financial capacities underpinned by existing rates."

Hydro One states on page 2 that, "The majority of capital expenditures for 2009 are a continuation of the projects and programs included in Hydro One's 2008 Distribution Rate Application that was previously filed with the Board."

- a) Please explain how the incremental capital request of \$174 million, the majority of which is comprised of "continuation of the projects and programs included in Hydro One's 2008 Distribution Rate Application," is consistent with the Board's statement that "the capital module is intended to be reserved for unusual circumstances."
- b) Please explain whether Hydro One considers its incremental capital request to represent "a 'targeted OM&A' or 'hybrid' form of IR." If so, please explain how this is consistent with the Board policy outlined in the Supplemental Report. If not, please explain how Hydro One's application is consistent with the comprehensive price cap form of incentive regulation ("IR") that has been espoused by the Board.
- c) Please justify Hydro One's approach to determine its proposed incremental capital investments by updating its entire capital plan submitted in EB-2007-0681, including storm damages, as opposed to determining which projects or part of projects should be considered incremental, as proposed by Oshawa PUC Networks Inc. in EB-2008-0205.

- d) Please identify which projects or part of projects among the planned 2009 capital additions are incremental, explaining why this is the case, and demonstrate that they are clearly non-discretionary,

4. Ref: 2009 3rd Gen. IRM Supplementary Filing Module (the "Sup. Module")

- a) Please provide the actual 2008 capital additions (or, if unavailable, the 2008 forecast capital additions) as well as additional information requested in column M of Sheet G2.1.
 - i) Please explain any difference between the 2008 actual capital additions and the test year amount of \$401 million.
 - ii) Please confirm whether any of the capital additions that were planned for 2008 will now be executed in 2009. If confirmed, please state what the total amount is and explain how it was treated for the purpose of deriving the incremental capital investment request.

5. Ref: Exhibit B1/Tab 3/Schedule 1/Pages 2 and 3

On page 2, Hydro One states that it has "considered the potential resulting impacts on OM&A expenditure levels," but also states on page 3 that "Hydro One Distribution, however, is not requesting any adjustments to OM&A levels in this submission. Overall impacts on OM&A costs will be addressed in Hydro One Distribution's next cost of service application."

On page 1 of Exhibit B1, Tab 3, Schedule 4, Hydro One indicates that the development capital investments consider "system configuration and additions in order to improve reliability."

On page 1 of Exhibit B1, Tab 3, Schedule 5, Hydro One indicates that "significant benefits can be achieved from the NMS and ORMS systems by enhancing the monitoring and control of the distribution network and improving the management of historical information." Other savings are highlighted on pages 3 and 4.

In Exhibit B1, Tab 3, Schedule 6, Hydro One describes the expected efficiency gains that will result from the Cornerstone project. On page 7, Hydro One states that "Savings will start to materialize in 2009 when it is anticipated that there will be \$3 million in savings attributable to incorporation of processes and utilization of the built in SAP functionality to support those processes."

- a) Please identify which projects as part of the overall 2009 capital additions are expected to result in savings and what those savings will be over the IR term.

- b) Please confirm whether Hydro One considers that the savings of the projects listed in a) will provide funding for these projects.
- c) Please confirm that Hydro One has deducted the expected \$3 million in savings resulting from the Cornerstone project in 2009 from the incremental capital investments requested, but has not netted the savings from the other projects identified in a). If confirmed, please explain why.
- d) Please explain how Hydro One's proposal to recover the revenue requirement associated with its requested incremental capital investments at this time, but address "overall impacts on OM&A costs" in Hydro One's next cost of service application is consistent with the comprehensive price cap form of IR that has been espoused by the Board in its July 14, 2008 *Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors*.

6. Ref: Exhibit B1/Tab 3/Schedule 6/Page 7

Table 4 shows the forecast 2009 savings arising from Cornerstone process improvements and the result of netting these savings against the total 2009 capital costs.

Please describe the forecasted savings over the whole term of 3rd Generation IR.

7. Ref: Exhibit B1/Tab 3/Schedule 6/Page 2

In light of the Board's findings in EB-2007-0681 with regard to the anticipated benefits associated with Cornerstone project over the term of the 3rd Generation IR, please justify any amounts sought for this project through the incremental capital module.

8. Ref: Exhibit B1/Tab 3/Schedule 6/Page 11

Hydro One is requesting \$0.6 million for a new Internal Energy Efficiency program for 2009.

- a) Please describe what improvements or measures would be implemented to build new facilities to a higher standard of energy efficiency.
- b) Please indicate what are the estimated savings over the IR term.
- c) Please provide a discounted cash flow analysis and the estimated pay back period for this project.

Letters of Comment

9. Ref: Letters of Comment Filed with the Board Secretary's Office

Your Notice of Application indicated that the letters of comment for your application will be part of the public record and be provided to the Board Members deciding the application. Board staff notes that, as of February 11, 2008, the Board Secretary's Office has received letters of comment from 20 interested parties.

- a) Please indicate whether Hydro One has responded to those letters of comment and, if not, if it intends to do so.
- b) If Hydro One has responded to the letters of comment, please provide a copy of your response to the Board Secretary's Office.
- c) If Hydro One has not responded, please provide Hydro One's position with respect to the issues raised in any un-answered letters.