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BY E-MAIL

May 28, 2012

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St, 27th Fl
P.O. Box 2319
Toronto, ON M4P 1E4

Dear Ms. Walli:

**Re: Hydro One Networks Inc.
Application for an Accounting Order to Establish an Incumbent Transmitter
Deferral Account
Board File No. EB-2012-0180**

In accordance with Procedural Order No. 1, please find attached Board staff's submission with respect to the subject proceeding.

Yours truly,

Original Signed By

Nabih Mikhail
Project Advisor, Electricity Facilities & Infrastructure



ONTARIO ENERGY BOARD

BOARD STAFF SUBMISSION

EB-2012-0180

**Request by Hydro One Networks Inc.
for an accounting order to establish a deferral account
related to the East-West Tie line proceeding (EB-2011-0140)**

May 28, 2012

A. Deferral Account Application and Proceeding

On March 22, 2012 Hydro One Networks Inc. (“HONI”) filed an application for an accounting order authorizing HONI to establish a new deferral account, the East West Tie deferral account (“EWTDA”) for the purpose of recording expenses relating to the East-West Tie Line proceeding (EB-2011-0140) and subsequent connection project-related activities for a new electricity transmission line. HONI proposes that the EWTDA be effective as of January 3, 2012.

HONI is requesting the deferral account to address three main categories of costs: OEB Allocated Proceeding Costs; Support Costs for OEB Designation Process; and Development Work Associated with Stations and Other Supporting Asset Expenditure.

The Board assigned File No. EB-2012-0180 to this application.

On April 18, 2012, the Board issued a Notice of Application and Written Hearing (“NOAWH”) and Procedural Order No. 1 (“PO1”), setting out the entities that the Board will adopt as intervenors in this proceeding and the criteria for cost eligibility. PO1 also provided a schedule for one round of interrogatories to be completed by May 14, 2012, intervenor and Board staff submissions to be filed by May 28, and reply submission by HONI to be filed by June 4.

B. Board Staff Submission

Board staff submits that it conditionally supports HONI’s application to establish a deferral sub-account in regard to the Support Costs for OEB Designation Process. The Board should decline the request by HONI for the other deferral sub-accounts to address the two cost categories: OEB Allocated Proceeding Costs; and the Development Work Associated with Stations and Other Supporting Assets. Board staff also submits that should the Board approve any of the deferral sub-accounts, the effective date should be March 22, 2012.

Board staff submits that it is premature at this time to comment on HONI’s proposed accounting entries with respect to regulatory accounting treatment of the requested sub-

accounts. The Board should address the specifics to the accounting entries for these sub-accounts at the accounting order stage, if and when the Board approves the establishment of the EWTDA.

The rationale for Board staff's submissions in regard to need addresses the three main categories of costs sequentially as presented in HONI's application.¹ Following that, Board staff addresses HONI's request for an effective date of January 3, 2012 for the EWTDA. The remainder of Board staff's submission is set out as follows:

- Section B.1 deals with OEB Allocated Proceeding Costs
- Section B.2 deals with Support Costs for OEB Designation Process
- Section B.3 deals with Development Work Associated with Stations and Other Supporting Asset Expenditure
- Section B.4 deals with HONI's request for an effective date of January 3, 2012 for the EWTDA, including all of its sub-accounts.

A summary of Board staff's submissions is included under Section C.

B. 1 OEB Allocated Proceeding Costs

Board staff notes that the first EWTDA sub-account HONI is applying for is a category of costs titled OEB Allocated Proceeding Costs. This category of costs includes cost awards to participants in the designation process, in addition to the Board's own costs.

Board staff also notes that HONI indicates² that the Board, in proceeding EB-2011-0140, determined that the OEB Allocated Proceeding Costs will be charged to the licensed transmitters. To validate that, HONI³ also referred to EB-2011-0140 Procedural Order No. 1, page 2, where it states in part that:

"The Board has determined that the costs of this proceeding, both cost awards to eligible intervenors and the Board's own costs, will be recovered from licensed transmitters whose revenue requirements are recovered through the Ontario Uniform Transmission Rates; namely Canadian Niagara Power Inc., Five Nations Energy Inc., Great Lakes Power Transmission LP, and Hydro One Networks Inc."

¹ HONI's Application and Evidence, March 22, 2012

² Exh. I/Tab I/Sch.4/pp. 1 -2 [HONI's response to Board staff Interrogatory #4, May 11, 2012]

³ Ibid, from page 1, lines 40 and 41 to page 2, lines 1 - 3

The costs will be apportioned between these transmitters based on their respective transmission revenues.”

HONI concludes by stating⁴ that:

“HONI is unaware of an alternative mechanism that is available for the OEB that would directly charge these costs through the UTRs.”

Board staff submits that there is an alternative mechanism which would occur at the conclusion of the EB-2011-0140 proceeding. As is normally followed in similar proceedings, Board staff expects that the following would occur:

- There will be steps for the eligible intervenors to file cost claims. The Board may then make findings and issue a Decision and Order on Cost Awards (“D&O CA”) where the amounts of these cost awards may be determined along with the amounts to reflect the Board’s own costs.
- The D&O CA may also determine if the noted total costs are material. If the costs are material, the D&O CA may include findings which would inform a future Board panel that would approve the updated UTR for the following year. The UTR are commonly updated annually, after considering and deciding on certain adjustments to the revenue requirements of each of the four licensed transmitters.

Board staff also notes that under the alternative approach, the three other licensed transmitters who will bear a portion of the OEB Allocated Proceeding Costs would be treated on the same basis as HONI. This is based on the fact that these three other licensed transmitters have not to date applied for a deferral account for this purpose.

Board staff therefore believes that the alternative approach presented above is appropriately transparent, and the Board should not approve HONI’s request for a deferral account for tracking the OEB Allocated Proceeding Costs.

However, should the Board decide to grant a deferral account for the “OEB Allocated Proceeding Costs”, Board staff believes that the Board could determine the characteristics of the account including such items as accrued interest, and the disposition of the account at the following UTR proceeding.

⁴ Ibid, page 2, lines 5-6

B. 2 Support Costs for OEB Designation Process

Board staff notes that the second EWTDA sub-account and category of costs HONI is applying for is Support Costs for the OEB Designation Process. HONI identified three types of costs that it will incur to support proceeding EB-2011-0140 for designation of an electricity transmitter. The three types of costs are:

- 1) Consultant cost;
- 2) Incremental administration cost; and
- 3) Labour cost.

HONI indicated that these three types of costs will not have their own sub-accounts but instead will be tracked separately through excel spreadsheets.⁵ In its pre-filed evidence HONI stated that:

“All of the above costs will be associated with providing technical information to the Board (and to the transmitter applicants via the Board) on transmission connection points, assisting with other transmission-related enquiries on an as-needed basis, and partaking as an intervenor in the EWT Line transmitter designation proceeding and the subsequent S.92 Leave to Construct proceeding, if required.”⁶

Board staff agrees with HONI that it may not be possible to fully anticipate the magnitude of the incremental costs that HONI may incur as an intervenor in the designation proceeding and whether HONI will need to engage these consultants. However Board staff submits that HONI is aware that there are seven parties engaged in the designation process and that the issues list for phase 1 of the designation proceeding has been approved earlier this year. This should allow HONI to estimate the incremental costs anticipated in that designation proceeding.

Board staff also agrees with HONI that materiality and prudence of the EWTDA balance will be subject to review at a future proceeding when HONI requests disposition of this account.⁷ Board staff notes that HONI confirmed that there is no guarantee of recovery of costs recorded in the EWTDA and its sub-accounts.⁸

⁵ EB-2012-0180, Response to VECC Interrogatory # 3.a) dated May 14, 2012

⁶ EB-2012-0180, Application and Evidence dated March 22, 2012, Section 3.1, Para2

⁷ EB-2012-0180, Response to Board staff Interrogatory # 3 dated May 14, 2012

⁸ EB-2012-0180, Response to Board staff Interrogatory # 1 dated May 14, 2012

Board staff submits that it disagrees with HONI's view⁹ that "Z-Factor Amount Eligibility Criteria" should not be used for the establishment of a deferral account. Board staff submits that causation, materiality, and prudence should be considered when establishing a deferral account.

Causation should be considered when setting up a deferral account as: the amounts to be recorded in the deferral account must be clearly outside of the base upon which base rates were derived; and moreover, the costs to be recorded in the deferral account should directly relate to the purpose of the account.

Materiality must also be considered when establishing the deferral account. The amount of the costs to be recorded in the account must be material in order to go through the effort of setting up a deferral account. Otherwise these costs should be expensed in the normal course.

The prudence of the costs recorded in the deferral account is primarily subject to review when disposition is requested. However, Board staff submits that it is important to consider the issue of prudence when considering setting up a deferral account.

Consultant Cost

HONI submits that it may have to engage external consultants to provide answers to inquiries about the reports produced by these consultants for HONI prior to the commencement of the designation process. HONI further submits that it cannot anticipate the quantity, the type, or if the parties will have questions that require the engagement of consultants.¹⁰

In response to Board staff interrogatory # 5, HONI provided a list of the consultants reports that it commissioned regarding the East-West Tie Line.¹¹ HONI also provided a list of other East-West Tie Line related information that it possesses.¹² (the "Second List"). The Second List included information regarding project definition, presentation of transmission projects, transmission maintenance practices, real estate data and historical outage data.

⁹ EB-2012-0180, Response to Board staff Interrogatory # 3, Question (a), dated May 14, 2012

¹⁰ EB-2012-0180, Response to Board staff Interrogatory # 2 dated May 14, 2012

¹¹ EB-2012-0180, Response to Board staff Interrogatory # 5 dated May 14, 2012, Table 1

¹² Ibid, Table 2

Regarding the consultants reports, Board staff is of the view that it is possible, subject to Board approval at that point in time, that these consultants reports may be referred to in the designation proceeding and if they are, it may require HONI to re-engage the consultants to provide further clarification or additional information. Board staff submits that the costs that HONI may incur in relation to these consultants reports should be eligible for inclusion in the Support Costs for OEB Designation Process sub-account. Board staff also submits that, in case the Board approves the recording of possible consultant costs, HONI should keep a log of the reports and related consultants that resulted in incurred costs so that such information is readily available in the future should the Board request it.

As noted above, the Second List¹³ provided by HONI includes reports, presentations, and other information that HONI is in possession of and that it may be asked questions on such reports and information during the designation proceeding. In Board staff's view, the costs of the items on this list are not incremental as HONI prepared these reports and information internally before the Notice of the designation proceeding was issued by the Board on February 2, 2012 (i.e., such costs are already being recovered through its current approved revenue requirement for the relevant test year).

Moreover, Board staff believes that if HONI is asked to provide further details on the documents in the Second List, it will do so using labour costs that are already accounted for in its revenue requirement. In conclusion, Board staff submits that the cost of providing information and responding to interrogatories related to the Second List is non-incremental to the designation proceeding and that the Board should not permit HONI to record those costs in the Support Costs for OEB Designation Process sub-account.

Labour Costs

Board staff notes that regarding labour costs, HONI indicated that it will track both incremental and non-incremental labour dedicated to the East-West Tie Line project.¹⁴ Board staff agrees with HONI that its non-incremental costs are already in HONI's current approved revenue requirement and so HONI will not seek recovery of these costs. Subsequently, HONI argued that by tracking these non-incremental costs from

¹³ Ibid, Table 2

¹⁴ EB-2012-0180. Application and Evidence dated March 22, 2012, Section 3.1 Para 4, (iii)

the outset, the costs will be readily available should the Board need information at a later date.¹⁵ Board staff deals with the issue of tracking incremental and non-incremental costs in the next section.

HONI submits that there is a possibility that providing support for the designation proceeding may result in heavy time demands on its staff such that there is a need to backfill a current position.¹⁶ Board staff submits that it is premature to speculate or comment on whether or not backfilling a current position is needed, but would see the benefit of recording these costs in the Support Costs for OEB Designation Process sub-account.

Tracking Incremental vs. Non-incremental Support Costs

As mentioned earlier, HONI is proposing to track both incremental and non-incremental labour costs in the Support Costs for OEB Designation Process sub-account. In its pre-filed evidence, HONI expressed its view that tracking non-incremental costs in this sub-account would ensure that such information would be available to the Board for possible use at a later date.¹⁷

In Board staff's view it is unnecessary to record non-incremental costs in the EWTDA as this adds undue complexity to the account considering that these costs can be tracked separately without being recorded in the EWTDA, as confirmed by HONI in its response to Board staff interrogatory #6.¹⁸ In that interrogatory response, HONI agreed with Board staff that it can track non-incremental labour costs without the use of the EWTDA. Further, HONI described a process for tracking these costs which would entail the use of time tracking sheets to record the number of hours worked and indicated that these documents would be made available upon request. HONI expressed that this methodology would ensure that non-incremental labour costs would be kept separate from incremental labour costs. Board staff agrees with HONI that it should implement the noted methodology.

¹⁵ EB-2012-0180, Application and Evidence dated March 22, 2012, Section 3.2 Para 1

¹⁶ EB-2012-0180, Application and Evidence dated March 22, 2012, Section 3.1, para 1

¹⁷ EB-2012-0180, Application and Evidence dated March 22, 2012, Section 3.2, para 1

¹⁸ EB-2012-0180, Response to Board staff Interrogatory # 6, Question (a), dated May 14

In conclusion, Board staff submits that it is reasonable to expect that HONI may incur consultant costs, incremental administrative costs, and possibly incremental labour costs. However, Board staff does not support recording non-incremental costs in the EWTDA as these costs can be tracked separately and therefore inclusion in the deferral account is unnecessary. If the above-mentioned costs are expected to be material, Board staff submits that the Board should approve the establishment of the Support Costs for OEB Designation Process sub-account as part of the EWTDA.

B. 3 Development Work Associated with Stations and Other Supporting Asset Expenditures

Board staff notes that the third EWTDA sub-account and category of costs for which HONI is applying is Development Work Associated with Stations and Other Supporting Asset Expenditures.

Board staff also notes that in response to question (a) of Board staff interrogatory # 7, HONI indicates¹⁹ that it has not incurred any development work costs to date associated with preliminary station and other supporting asset work.

Board staff agrees with HONI's response to question (b) item 3(c) of Board staff interrogatory # 3, indicating that²⁰ the "Development Work Associated with Stations & Other Supporting Asset Expenditures" and associated costs would end once section 92 approval is received for the designated transmitter.

Board staff, in its interrogatory # 8, explored two alternatives²¹ to HONI's request for a deferral account to cover the costs of Development Work Associated with Stations and Other Supporting Asset Expenditures.

Board staff submits that these two noted alternatives are workable, and each addresses the concerns raised by HONI in its Application²² where it stated in part that:

"The risk profile of these costs is different from that of [HONI's] normal capital construction activities as, unlike other projects, [HONI] is not managing this

¹⁹ Exh. I/Tab 1/Sch.7/pp. 1 - 3 [HONI's response to Board staff Interrogatory #7, May 11, 2012]

²⁰ Exh. I/Tab 1/Sch.3/p. 3/Question (b) 3. c. [HONI's response to Board staff Interrogatory #3, May 11, 2012]

²¹ Exh. I/Tab 1/Sch.8/pp. 1 - 3 [HONI's response to Board staff Interrogatory #8, May 11, 2012]

²² HONI's Application and Evidence, March 22, 2012/sec. 4.1/p. 6

project or the approval process. As a result, [HONI] does not have the level of accounting assurance that the project will ultimately proceed and go in-service that it requires in order to capitalize these amounts under generally accepted accounting principles. To meet the required in-service date of the EWT Line, station development work needs to commence prior to the designated transmitter receiving its S.92 approval.”

Any one of the two proposed Board staff alternatives would allow HONI to require a reasonable security deposit from the eventual designated transmitter to guard against risks outlined in HONI’s application, and quoted above for clarity.

HONI’s response Re Board staff proposed Alternative 1

Board staff framed an alternative to relying on a deferral account, by posing question (a) of interrogatory # 8. In that interrogatory Board staff requested²³ that HONI indicate whether or not it would include in its agreement with the designated transmitter, as required by section 6.8 of the Transmission System Code (“TSC”) on agreements between neighbouring transmitters, conditions requiring reasonable security deposit from the designated transmitter to guard against risks it outlined in its Application (“Alternative 1”).

HONI’s responded²⁴ to the noted Alternative 1 by stating that:

“HONI notes that Section 6.3.10 of the TSC applies to customers only. As such, HONI cannot compel a neighbouring transmitter to accept the conditions in Section 6.3.10 in an agreement and therefore remains of the view that it would be more prudent to proceed with the requested deferral sub-account.”

Board staff believes that since HONI feels that on its own it is not able to conclude an agreement with the designated transmitter to address the noted risks, the Board should consider including in its order a direction for HONI. Such a direction may require HONI to include in its agreement with the designated transmitter terms that address HONI’s requirement for security deposits or similar security vehicles. Security deposits or similar security vehicles would guard against the noted risks identified by HONI in its application.

²³ Exh. I/Tab 1/Sch.8/p2/Question(a) and response [HONI’s response to Board staff Interrogatory #8, May 11, 2012]

²⁴ Ibid

HONI's response Re Board staff proposed Alternative 2

Board staff framed a second alternative to relying on a deferral account, by posing question (c) of Board staff interrogatory #8 and requesting²⁵ HONI's comments on the view that under section 70 (2) (c) of the Act, the Board can amend HONI's transmission licence ("Alternative 2"). Such amendment could require HONI to enter into an agreement with the eventual designated transmitter where a reasonable security deposit can be arranged. Security deposits would guard against risks that HONI outlined in its application.

HONI's response indicated that it concurs that the Board appears to have such authority.

Board staff submits that the Board should consider choosing one of the two noted alternatives, as opposed to granting a deferral account to deal with HONI's noted risks for the "Development Work Associated with Stations and Other Supporting Asset Expenditures", as these are viable alternatives to help mitigate potential risks that HONI may face.

B.4 Effective Date of the EWTDA

Board staff notes that:

- On February 2, 2012, the Board issued a Notice of Proceeding for the designation process.²⁶ The Notice of Proceeding invited all transmitters who registered their interest in the designation process to file a plan for the development of the East-West Tie Line. In Board staff's view, this marked the start date of the designation proceeding.
- HONI's response to London Property Management Association's ("LPMA") interrogatory #1, provides its justification for the January 3, 2012 effective date for the EWTDA by stating that:

"On August 12, 2011 Board Staff sent a letter to licensed transmitters and other interested parties to indicate their interest in filing a development plan. Since this notification, meetings and consultation have occurred between Board Staff and potential

²⁵ Ibid, Question(c) and response

²⁶ EB-2011-0140, Notice of Proceeding dated February 2, 2012

transmitters which HONI has attended.”²⁷

- In response to LPMA's interrogatory # 2, HONI indicates that it had not incurred any incremental costs for the proposed EWTDA from January 3, 2012 to March 22, 2012. HONI argues that there may be costs incurred as a result of the August 12, 2011 Board staff letter, which may be recoverable through the UTR i.e., costs of the first category - the OEB Allocated Proceeding Cost.
- HONI also indicates that while it had not incurred any incremental costs²⁸ from January 3, 2012 to March 22, 2012²⁹, it incurred non-incremental³⁰ costs of \$50,000 related to the designation proceeding in the same period.³¹

Board staff submits that the effective date for deferral account if granted should be March 22, 2012, based on the following facts:

- Any costs that may predate that date and are attributable to the first category of costs i.e., OEB Allocated Proceeding Costs, can be tracked. These costs relate to cost claims by intervenors and may be subject to a potential future proceeding – normally that step may occur at the conclusion of the East-West Tie Line proceeding (EB-2011-0140);
- Events such as meetings between Board staff, consultants and staff of HONI that occurred between August 11, 2011 and issuance of the Notice on February 2, 2012 were exploratory and preliminary³² in nature and should not be classified as incremental. In addition HONI indicated that it had not incurred any incremental costs from January 3, 2012 to March 22, 2012.³³

C. Summary of Board Staff Submissions

Board staff submits that the effective date for deferral account, if granted, should be March 22, 2012, as outlined in section B.4 of this submission.

²⁷ EB-2012-0180, Response to LPMA Interrogatory # 1a) dated May 11, 2012

²⁸ Incremental costs are costs HONI classifies in its Application as not included in its 2012 approved transmission revenue requirements

²⁹ EB-2012-0180, Response to LPMA Interrogatory # 2a), p. 1, lines 15 – 16, dated May 11, 2012

³⁰ Non-incremental costs are costs HONI classifies in its Application as included in its 2012 approved transmission revenue requirements.

³¹ EB-2012-0180, Response to LPMA Interrogatory # 2a), p.1, lines 28 -30 dated May 11, 2012

³² EB-2012-0180, Response to LPMA Interrogatory # 1a), p. 1, lines 20 - 25 dated May 11, 2012

³³ EB-2012-0180, Response to LPMA Interrogatory # 2a), p. 1, lines 15 – 16, dated May 11, 2012

Board staff submits that in regard to HONI's request for a deferral account for tracking the OEB Allocated Proceeding Costs, the Board should instead deal with these costs at the conclusion of the East-West Tie Line designation process (EB-2011-0140), as outlined in section B.1 of this submission.

Boards staff agrees in principle with HONI's request for a deferral account for tracking Support Costs for the OEB Designation Process. Board staff expects HONI to estimate the expected costs under this category in spite of the uniqueness of the designation proceeding as outlined in Section B.2 of this submission. Board staff also agrees with HONI that materiality and prudence of the EWTDA balance will be subject to review at a future proceeding when HONI requests disposition of this account.³⁴ Board staff notes that HONI confirmed that there is no guarantee of recovery of costs recorded in the EWTDA and its sub-accounts.³⁵

Board staff submits that Board should consider choosing one of two alternatives set out in section B.3 of this submission, instead of HONI's request for a deferral account to deal with Development Work Associated with Stations and Other Supporting Asset Expenditures:

- Alternative 1 requires that the Board consider including in its order a direction for HONI to include in its agreement with the designated transmitter, terms that address HONI's requirement for security deposits or similar security vehicles to guard against the noted risks identified by HONI in its application.
- Alternative 2 requires that the Board consider amending HONI's transmission licence to require HONI to enter into an agreement with the eventual designated transmitter where reasonable security deposit can be arranged to guard against risks that it outlined in its application. This is premised on section 70 (2) (c) of the Act, where the Board can amend HONI's transmission licence.

All of which is respectfully submitted.

³⁴ EB-2012-0180, Response to Board staff Interrogatory # 3 dated May 14, 2012

³⁵ EB-2012-0180, Response to Board staff Interrogatory # 1 dated May 14, 2012