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Ontario

BY E-MAIL

November 12, 2012

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Board Staff Questions for the Technical Conference: November 12, 2012
Hydro One Networks Inc.
2013 Electricity Distribution Rates
Board File No. EB-2012-0136

Please find attached Board staff questions and areas of interest for the Technical Conference to be held on November 22, 2012.

Sincerely,

Original Signed By

Harold Thiessen
Case Manager – EB-2012-0136
Senior Advisor - Applications

Attachment

Hydro One Distribution 2013 Rates
EB-2012-0136, Board Staff Questions for the Technical Conference
November 12, 2012

Board staff will have Technical Conference questions requesting additional information and clarification in the following areas:

1) Ref: Exhibit I/Tab2/Schedule 1.01 Staff 2
On page 2 of 7 at line 26:

a) When did the vendor of the current CIS stop supporting the product?

b) Who has provided support in the interim period since the vendor stopped supporting the product?

c) What was the plan to support the product in the years beyond 2013 prior to the decision that the system should be replaced in 2013?

2) Ref: Exhibit I/Tab2/Schedule 1.01 Staff 2
On page 3 of 7, lines 11-16:

Hydro One indicates that there is great risk in making changes to the core programs that make up the application.

a) Please indicate how these changes have been made for recent evolution such as time of use and smart metering, including identifying whether it was done by the vendor or by staff or by other parties, and what difficulties were experienced.

b) What changes are known to be occurring in the period between the new proposed in-service of the CIS and that which was anticipated at the most recent rate hearing?

c) What plans were in place to deal with those changes referred to in b)?

3) Ref: Exhibit I/Tab2/Schedule 1.01 Staff 2
On page 4 of 7, line 34:

The alignment with outsourcing strategy indicates the belief that the costs for maintenance for the new system will be less than that of the current system.

a) Is there any evidence to suggest that the current suppliers will not be amenable to providing better prices if their user base is declining? Are they not more likely to be amenable to lower pricing than suppliers in a growing market where skilled programmers may be in scarce supply?

b) Has Hydro One obtained some estimates of the different costs for maintenance and service of the new and existing systems? If so, please provide these estimates.

c) Is Hydro One subject to any contractual costs for “early” conversion to the new system and therefore not making use of the contracted services with Inergi? Please detail. How have such costs been taken into account?

4) Ref: Exhibit I/Tab2/Schedule 1.01 Staff 2

On page 7 of 7:

a) At line 11, Hydro One indicates that it “believes the Board will see fit to make the appropriate award for the necessary incremental investments”.
Has Hydro One made no contingency plan for the situation if the Board approves anything less than 100% of the revenue requested to fund the increased rate of replacement of substations? transformer spares? Wood poles?

b) At line 1 Hydro One indicates “Hydro One has continued to spend funds in line with the original award for substantially similar work.” Does this mean that the CIS project work is continuing on the basis of the 2016 in-service?

5) Ref: Exhibit I/Tab2/Schedule 1.04 Staff 5

Hydro One indicates that additional costs will be incurred under ‘harvesting of assets” conditions. Can Hydro One provide an estimate or forecast of the additional costs? How much more expensive is unplanned work outside of work hours?

6) Ref: Exhibit I/Tab2/Schedule 1.06 Staff 7

On page 2 of 3:

a) At d) Hydro One indicates it “believed that use of the 2010 actual for comparison to 2011 was appropriate.”
Why did Hydro One consider this more appropriate?

b) If the Board finds that the actual 2011 revenue was more appropriate, would the threshold level be exceeded? Please calculate the threshold value that would result and provide the detailed calculation.

7) Ref: Exhibit I/Tab2/Schedule 1.07 Staff 8

On page 2 of 3:

At line 28, Hydro One explains why depreciation should be included in an assessment of whether or not the threshold value is exceeded: “Depreciation of $283M was included in the original award but ICM 2013 calls for in-servicing of $414M. Therefore, upon completion of the planned spending, Rate Base will grow in 2013 by $131M.”

a) Please explain why including the depreciation for the in-serviced asset along with the capital value of the asset being placed in service does not over-value the assets which are being placed in service in 2013? Why should this be a consideration over and above the actual capital expenditure in the determination of the threshold value for ICM 2013?

b) Should the depreciation not be recovered in the following year? Does including depreciation in rate base not represent an inappropriate increase in the capital expenditure that is being compared with the threshold value?

c) How is the addition of the depreciation in assessment of the threshold value consistent with the Board's statement (quoted at line 5) that "… adjustment in rates will be linked solely to the costs of the incremental capital."

d) In the analogy example quoted by Hydro One in part d) of the response on page 3, Hydro One provides an example of a $400 asset which is depreciated on a straight line accounting basis and compares this with the replacement cost of the asset which price has escalated to $880 on a compound basis and shows that they are not equivalent amounts.

   i) For this analogy, would Hydro One at the time of the rate hearing in 1972 have applied to the Board for a rate increase on the basis of a capital expenditure of $880? Would that be an appropriate description of the capital expenditure requirement at the time?

   ii) Is Hydro One suggesting that depreciation should represent the full amount of inflation in each year?

   iii) Does Hydro One agree that the proposed approach is not consistent with accounting practice in the rest of the province? Is this an issue which Hydro One should be arguing before a forum on accounting principles rather than at the Board?

   iv) There are many assets (e.g. wood poles) that have been in useful service beyond their years for which depreciation was recovered, and which could be considered as "over-funded" and which should now be deducted from the rate base in this application. Would Hydro One concur that it would be appropriate for these depreciated assets to be taken into account at any point where there is a claim based on the fact that depreciation is not equal to expenditure? Does this imply that Hydro One is recalculating (deducting from) the rate base by recognizing assets which have been fully depreciated but which are still providing useful service and a continuing revenue stream?

   v) Would this not lead to the conclusion that no new capital expenditure authorization would ever be needed for replacement because Hydro One would have the full capital in hand when replacement of assets is required?

   vi) Would this example represent an inter-generational transfer allocation, since revenue would be being recovered from current customers to fund future price escalation?

8) Ref: Exhibit I/Tab2/Schedule 1.09 Staff 10
On page 3 of 4:

At line 4, part g) of the response, Hydro One indicates that the work required to be done for the increased rate of pole replacement would make use of the labour currently applied to the smart meter program, which is coming to an end. Is the skill set of those working on the smart meter program the same as that which would be required for pole replacement?

9) Ref: Exhibit I/Tab2/Schedule 1.10 Staff 11
On page 2 of 2:

a) The responses suggest that there is not a clear plan on how the problem of defective poles is being dealt with. If, as indicated in part g) (line 38) there is a means of "carefully targeting poles for replacement to maintain an acceptable level of risk on the system and plans to increase replacement rates in years beyond 2013 to deal with the issue.", why is it not being done in 2013?

b) What is the long term plan for pole replacement that will replace the defective pole problem and will provide the replacement rate that Hydro One claims to be targeting?

10) Ref: Exhibit I/Tab2/Schedule 1.11 Staff 12
On page 3 of 5:

a) Please provide a more comprehensive and detailed response to the original questions a) and b).
b) Please reconcile the EB-2009-0096 evidence (Exhibit D1/Tab 3/Sch2/pg.4) for Stations Sustaining capital to the $3.2 million and $25.8 million found in the response provided in the original c).

c) In the response to k), Hydro One indicates that the cost of refurbishment of 23 used transformers would cost $3.5 million as opposed to the cost of purchasing new spares of $13.3 million. How does Hydro One then justify the significant additional cost of purchase over refurbishment?

11) Ref: Exhibit I/Tab8/Schedule 1.01 Staff 23

a) Hydro One applied for the PILs allowances for the service areas of the acquired distributors in 2001 and 2002 in a similar way to the former MEUs. Why would Hydro One assume that there is no need to deal with any PILs variances that have arisen?

b) Does Hydro One have a Board decision or order exempting it from accounting for PILs variances for the period 1999 through April 30, 2006 or from using Account 1562?

c) Hydro One accounted for PILs variances in its tax deferral account for both distribution and transmission businesses. Hydro One was given approval to clear balances from time to time from this tax deferral account. Did Hydro One identify and differentiate between Account 1562 and Account 1592 in its PILs disposition evidence in prior applications? Please provide the case and evidence references.

d) The Board has a policy and process for accounting for the decline in income tax rates and changes in tax rules. For electricity distributors, this policy was published in 2001. Why does Hydro One assume that it is exempt from accounting for the decline in income tax rates and changes in tax rules during the period 1999 through 2005?

e) Did Hydro One account for any changes in income and capital tax rates, exemptions and rules during the period 1999 through 2011?

    i) When did Hydro One start to account for these tax changes?
    ii) Why does Hydro One distinguish between the rate periods regarding when the Board's PILs regulatory policy applies and does not apply?

12) Ref: Exhibit I/Tab8/Schedule 1.03 Staff 25

In this response, Hydro One included a revised Attachment 1 which showed an updated DVA continuity schedule.

- In the revised Attachment 1, it appears that the Column "Transactions Debit/ (Credit) during 2010 excluding interest and adjustment" was reduced by the amount that was approved for disposition in 2010 [EB-2009-0096] for each deferral/variance account, as compared to the same column in the pre-filed DVA continuity schedule. A similar adjustment was also made in the 2010 carrying charge section of the DVA continuity schedule.

- It appears that in the revised Attachment 1, the amount that the amount the Column "Transactions Debit/ (Credit) during 2010 excluding interest and adjustment" was reduced by was recorded in the Column "Adjustments during 2010 – other". A similar adjustment was also made in the 2010 carrying charge section of the DVA continuity schedule.

It is not clear to Board staff from reviewing the revised DVA continuity schedule if the journal entry to transfer the 2010 Board approved amount from each deferral/variance account to Account 1595 was actually done in 2010.

Please provide a copy of the journal entry (both sides – debits and credits) that shows the transfer to Account 1595 from each deferral/variance account for the amount approved for disposition in 2010 (principal and carrying charges), EB-

2009-0096. Please ensure that the journal entry shows the date the entry was made to the general ledger.

13) Ref: Exhibit I/Tab8/Schedule 1.05 Staff 27

In this response, Hydro One indicated that it is attempting to estimate line losses experience on the system and that such an estimation is based on a system assessment. Hydro One stated that the calculation requires that the data be linked to the actual time that the energy was provided. Hydro One articulated that it is attempting to track the dollar value of the variance but that nothing has been recorded in the general ledger to date.

Board Decision EB-2009-0096, which directed Hydro One to track the dollar value of variances between the Board approved losses recovered in rates and actual line losses, commencing January 1, 2010, was issued on April 9, 2010.

a) Please confirm if Hydro One has been tracking the dollar value of variances between the Board-approved losses recovered in rates and actual line losses, as per the EB-2009-0096 decision. Please state the effective date of tracking these values and where these variances are being tracked. If the dollar value of such variance is not being tracked, please explain.

b) Please clarify what Hydro One means by "attempting" to track the dollar value of such variance. Please explain.

c) If Hydro One has been tracking the dollar value of such variance, please provide a status update and more details, including the dollar value of the variance as at September 30, 2012.

d) Please explain why Hydro One has not recorded an estimate for the variance in its general ledger from 2010 through 2012. Please indicate why such a variance has not been recorded in Account 1588, particularly since other estimates are recorded in Hydro One's general ledger and audited financial statements at year-end (e.g. unbilled revenue).