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October 27, 2014

Our File Number: 72738

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street
Suite 2700, P.O. Box 2319
Toronto, ON M4P 1E4

Dear Ms. Walli:

**Re: Hydro One Networks
2015-2019 Distribution Custom Rate Application (EB-2013-0416)
Licence Requirement Exemption (EB-2014-0247)**

Please find Hydro One's reply argument in EB-2013-0416. Hydro One's submissions on the exemption requested in EB-2014-0247 are found at the conclusion of its main reply.

Yours very truly,

ORIGINAL SIGNED BY DONALD H. ROGERS

Donald H. Rogers, Q.C.
DHR:db

HYDRO ONE NETWORKS CUSTOM IR FOR

DISTRIBUTION RATES 2015-2019

EB-2013-0416

&

HYDRO ONE EXEMPTION REQUEST

EB-2014-0247

HYDRO ONE NETWORKS INC.

REPLY SUBMISSION

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OVERVIEW

Hydro One Networks (“Hydro One”) applied to the Board for an order approving the revenue requirement, cost allocation and rates for its distribution business for the years 2015 through 2019 (“the test years”) under assigned docket number EB-2013-0416.

Following its application, interrogatories, technical conferences and a settlement conference, Hydro One delivered its closing argument in chief orally to the Board on September 24, 2014. Board staff delivered its submissions on October 7, 2014, with intervenors’ arguments provided by October 15, 2014.

This is Hydro One’s reply submission. This document is complementary to the oral argument referenced above. The purpose of this reply is to respond in detail to the central arguments made by the Ontario Energy Board staff (“Board staff”) and the intervenors, without simply summarizing or repeating the vast body of documentary and oral evidence that has already been put forth.

Hydro One will first outline its position on matters which emerged as central themes in the proceeding and in the arguments:

- the extensive reductions to revenue requirement urged by Board staff and intervenors;
- the form of this application, including productivity and benchmarking; and
- denial of actual smart meter costs prudently incurred.

Hydro One will then outline its submissions on each of the matters outlined in accordance with the Board’s approved issues list, but will not be repetitive in its argument where specific issues have been addressed within the more central issues.

Given the length and breadth of the submissions received by Board staff and intervenors, not each and every point has been commented upon. Silence however is not tantamount to acceptance or agreement by Hydro One.

Hydro One received final responding arguments from the OEB staff and the following intervenors:

- Association of Major Power Consumers of Ontario (AMPCO)
- Balsam Lake Coalition (Balsam Lake)
- Canadian Manufacturers and Exporters (CME)
- City of Hamilton (Hamilton)
- Consumers Council of Canada (CCC)
- Energy Probe Research Foundation (Energy Probe)
- Federation of Ontario Cottagers' Associations (FOCA)
- Green Energy Coalition (GEC)
- Independent Participant – Patrick Hurley
- Power Workers' Union (PWU)
- Ontario Federation of Agriculture (OFA)
- School Energy Coalition (SEC)
- The Society of Energy Professionals (SEP)
- Sustainable Infrastructure Alliance of Ontario (SIA)
- Vulnerable Energy Consumers' Coalition (VECC)

INTRODUCTION

Hydro One was the first electricity distributor to come forward following the release of the *Report of the Board – Renewed Regulatory Framework for Electricity Distributors: A Performance Based Approach* (RRFE) with a Custom IR application to set distribution rates. During the development of this custom application, Hydro One conducted extensive stakeholdering, far more than any utility has done in the past, to obtain input from interested parties into the presentation of this unique rate application.

Hydro One addressed stakeholder feedback and suggestions in its original pre-filed evidence, evidentiary updates, numerous technical conferences and interrogatories, during an oral presentation to the OEB, as well as during the oral hearing.

As in all quasi-judicial proceedings, there are some points of disagreement and legitimate areas of debate, depending on the participant's unique interests. Hydro One has done its best to present a complete application, balancing the interests of the ratepayers and the utility alike, and in accordance with the RRFE.

Hydro One believes that it has provided a complete application with sufficient evidence that permits the Board to set just and reasonable rates for the distribution of electricity from 2015-2019 that is in keeping with the intent and spirit of the RRFE.

It is important to highlight for the Board at the outset what is being sought over the 5 year plan. Hydro One is seeking a 3.2% increase in OM&A over the 5 year term, or 0.6% per year and a 7.1% increase in capital spending over the 5 year terms, or 1.4% per year. The proposals for both OM&A and capital are below the actual Bank of Canada rate of inflation of 2% or the Board inflation rate of 1.7%.

APPROVALS REQUESTED

The list of approvals that it is seeking from the Board has been updated for the purpose of this final submission and is outlined below:

Revenue Requirement

1. An order pursuant to Section 78 of the *Ontario Energy Board Act* approving 2015 – 2019 revenue requirement and customer rates for the distribution of electricity to be implemented/effective on January 1 of each test year.
2. Approval of a distribution revenue requirement as set out in Exhibit E2-1-1 of \$1,415M for 2015, \$1,523M for 2016, \$1,578M for 2017, \$1,615M for 2018 and \$1,660M for 2019.
3. Approval of operations, maintenance and administration (OM&A) expenditures of \$564.3M in 2015, \$610.2M in 2016, \$614.0M in 2017, \$603.9M in 2018 and \$600.0M in 2019. Details of Hydro One's OM&A expenditures are itemized in Exhibit C2-2-1 and discussed in written direct evidence in the schedules contained within Exhibit C1-2.
4. Approval of total capital expenditures and in-service additions. Capital expenditures are forecast to be \$648.9M in 2015, \$654.7M in 2016, \$661.4M in 2017, \$655.1M in 2018 and \$669.1M in 2019. Details of Hydro One's capital expenditures are provided in schedules filed at Exhibit D2-2 and discussed in detail in the schedules contained within Exhibit D1-3. Capital in-service additions are forecast to be \$656.6M in 2015, \$621.8M in 2016, \$696.0M in 2017, \$681.4M in 2018 and \$660.9M in 2019 as described in Exhibit D1-1-2.

5. Further, approval of the inclusion of in-service assets as shown in Exhibit D1-1-1, Table 3 totaling \$564.9M previously recorded as regulatory assets for smart meters, smart grid and distributed generation into rate base effective January 1, 2015.
6. Approval of Hydro One Distribution's rate base of \$6,533M in 2015 which includes projects approved for interim funding as part of the Incremental Capital Module approved by Board in EB-2012-0136, \$6,864M in 2016, \$7,191M in 2017, \$7,541M in 2018 and \$7,870M in 2019 as discussed at Exhibit D1-1-1.
7. Approval of depreciation and amortization expense of \$355.4M in 2015, \$374.9M in 2016, \$390.2M in 2017, \$402.9M in 2018 and \$413.6M in 2019 as discussed in Exhibit D1-1-1 and further detailed in Exhibit C2-4-1.
8. Approval to recover regulatory assets with a net balance of \$33.2M to be collected over a 5 year period at \$6.6M per year as updated in Hydro One's Argument in Chief¹ including:
 - a. The final disposition of the smart meter costs recorded in the Minimum Functionality (1555) and Exceeding Minimum Functionality (1556) variance accounts. Hydro One is seeking the cost recovery associated with actual smart meter activities from 2009 through 2013 and forecast activities through 2014 as requested by Board staff during the proceeding;²
 - b. Smart Grid assets up to December 31, 2013; and
 - c. Assets to facilitate Distributed Generation up to December 31, 2013.

¹ Transcript Vol VIII, pg 18

² TC Transcript Vol 1, pg 67

9. Approval of the establishment of two new deferral/variance accounts effective January 1, 2015: Bill Impact Mitigation Variance Account; and Rate Smoothing Deferral Account.
10. Approval of the continuation of the following deferral accounts: Tax Rate Changes Account; and Pension Cost Differential Account.
11. Approval to discontinue (booking additional principal amounts to the account balances) the following regulatory accounts effective January 1, 2015:
 - a. Smart Meter- Minimum Functionality;
 - b. Smart Meter – Exceeding Minimum Functionality;
 - c. Distributed Generation – Other Costs – Hydro One Networks Inc. (HONI) – Variance Account;
 - d. Distributed Generation – Express Feeders – HONI – Variance Account;
 - e. Smart Grid Variance Accounts;
 - f. Distribution System Code (DSC) Exemption Deferral Account;
 - g. Deferred Revenue Project Costs Variance Account (2009);
 - h. Generator Joint Use Revenue Variance Account;
 - i. Special Purpose Charge Variance Accounts (1595 – Recovery of Regulatory 12 Balances Account – Sub Account)
 - j. Microfit Connection Charge Variance Accounts (1508 – Other Regulatory Assets – 14 Sub Account); and
 - k. OEB Cost Differential Account.
12. Approval of the proposed additional components of the Custom Application:
 - a. The proposed Annual Adjustment Mechanisms;

- b. The proposed Adjustments Outside of Normal Course of Business;
- c. The proposed Off-Ramp conditions; and
- d. The proposed Annual Outcome Measurement Reporting as provided in Undertakings J4.8 and J5.7.

Cost Allocation and Rates

13. Approval for the following rate-related adjustments:

- a. Reclassification of customers to reflect the findings of the review of existing customer rate classification;
- b. The addition of a new “Unmetered Scattered Load” rate class;
- c. To increase the amount of revenue collected via fixed charges;
- d. To move the revenue-to-cost ratios for all rate classes to within the range of 98% - 102% over the 5 year period;
- e. Adjustments to reflect the Board directed line loss study;
- f. Proposed rate mitigation plans for some customers moving between rate classes in accordance with the results of the rate class review.

14. Approval of new Retail Transmission Services Rates to reflect the Board’s approval of new Uniform Transmission Rates effective January 1, 2014 per its decision in EB-2012-0031.

15. Approval of 2015 rate schedules including terms and conditions of service as set out in Schedule 1 of Exhibit G2-2 which incorporate Hydro One distribution’s proposed Retail Transmission Service Rates and loss factors.

16. Approval of charges for the provision of miscellaneous services set out in Exhibit G2-5-1.

17. Approval of the establishment of a rate rider to implement its proposed rate smoothing deferral account over the 2015 – 2019 period as described in Exhibit F1-1-2.
18. Approval of Hydro One's proposed cost allocation and rate design methodology, including modification to the Board's cost allocation model as described in Exhibit G1-1-1 and Exhibit G2-1-1 and supported by the balance of the evidence contained in Exhibit G.
19. Approval of Hydro One's revised line loss factors as described in Exhibit G1-8-1.
20. A declaration that the current rates be approved as interim rates pending implementation of 2015 distribution rates to be effective January 1, 2015.

Exemption Request in EB-2014-0247

1. Approval for a licence exemption from section 7.5.2 of the DSC as it applies to section 7.5.1 of the DSC. Section 7.5.1 directs distributors' obligation respecting missed and re-scheduled appointments with customers. Section 7.5.2 requires that these obligations be met 100% of the time on an annual basis. Hydro One asks that the Board grant an exemption, on a permanent basis from the 100% requirement. Details supporting this request are set out in Exhibit A-18-1 Appendix A. This exemption was made under EB-2014-0247, but is being addressed as part of the within application.

Hydro One submits that its proposals are responsible and demonstrative of prudent management, customer focus and embedded efficiencies and productivity gains.

HYDRO ONE'S 2015 TO 2019 REVENUE REQUIREMENT

i. Factors contributing to the Year over Year increase in revenue requirement

Intervenors expressed concerns about the overall increases in revenue requirement.

The table below shows the breakdown of increases in revenue requirement for each year³.

	2011	2015	2016	2017	2018
	to	to	to	to	To
	2015	2016	2017	2018	2019
Change in OM&A	1.9%	3.1%	0.2%	-0.6%	-0.2%
Rate Base Growth	9.8%	3.3%	2.3%	2.3%	2.3%
Change in Cost of Capital	-1.1%	0.9%	0.6%	0.4%	0.6%
External Revenue	0.0%	-0.1%	-0.1%	0.0%	0.0%
Other	-0.1%	0.1%	-0.2%	-0.1%	0.0%
Total Change	10.5%	7.3%	2.9%	2.1%	2.6%

The primary driver impacting the increase in revenue requirement over the 2015 - 2019 test years is significant growth in the rate base, clearly shown in the table above. Rate base grew significantly from 2011 to 2015 given the large number of capital assets that were placed into service during this time, an IRM period. Further change is impacted by the forecast capital work program during 2015 to 2019, the driver behind a custom rate application, not a formulaic rate setting approach.

³ Table 7, Exhibit E1-1-1; Undertaking Response J2.1

The overall change in OM&A is minor and even decreases in 2018 and 2019, with an average increase of 0.6% per year, well below the rate of inflation. This is due to the productivity savings embedded in the plan. Board Staff and VECC recognize that Hydro One's OM&A costs are reasonably controlled over the plan.

Hydro One believes it is prudent to carry out the planned work programs to meet its objectives of addressing customers' needs; managing service quality and reliability; ensuring public and employee safety; and meeting system growth and asset end-of-service life requirements as well as meeting the Board's objectives of the RRFE.

ii. Revenue Requirement Impact of the Recommended Reductions in Work Programs by Board staff and Intervenors

Board staff and intervenors expressed concerns about revenue requirement, program costing and level of work proposed by Hydro One. How to address those concerns was presented in varying fashions.

Some, like Board staff and VECC did not identify any reductions to specific work programs. In other words, the OM&A and capital programs underpinning this custom cost of service application were not challenged.

SEC primarily and others challenged many of the work programs and urged varying reductions on that basis. Key areas where reductions were urged include compensation, vegetation management and pole replacement.

Board staff and certain intervenors urged introduction of a formulaic stretch factor, a principle inconsistent with a custom application. In doing so, these parties referenced

the PEG report which includes an extreme stretch factor of 0.6%, applicable to only 5 distributors including Hydro One.⁴ Hydro One calculated its “stretch factor” of 0.29% at the parties’ request. However, these two figures cannot be directly compared as the PEG stretch factor applies before any incremental capital is added. The 0.29% figure was calculated relying upon the entire work program, OM&A and capital.

Board staff initiated the concept that a stretch factor significantly higher than the PEG report was appropriate, ignoring the embedded savings, an admittedly arbitrary proposition. The result is a punitive stretch factor, more than double what the Board’s own expert recommended was appropriate for a 4th GIRM application.⁵

This concept was then adopted by others, and taken even further by some like CME which urged that the Board impose a 2% stretch factor, again ignoring the embedded savings. The result is a stretch factor that is more than almost 4 times as high as that proposed in the PEG report.

Some intervenors argued even further to the extreme, including AMPCO, CCC, CME and SEC, and recommended that the Board not only order extensive reductions to the capital and OM&A work programs, but also impose a punitive stretch factor further reducing the revenue requirement.

Hydro One has summarized the cumulative impact of the most significant reductions recommended by intervenors on its revenue requirement over the test years in the table below, with details by intervenor provided in Appendix “A”:

⁴ PEG report – Empirical Research in Support of Incentive Rate-Setting: 2013 Benchmarking Update

⁵ 1% proposed + 0.29% embedded in application = 1.29%

\$ M	2015	2016	2017	2018	2019
Hydro One Proposed	\$1,415	\$1,523	\$1,578	\$1,615	\$1,660
Intervenor Proposal – Most punitive	\$1,369	\$1,376	\$1,410	\$1,436	\$1,454
Net annual difference %	-3%	-10%	-11%	-11%	-12%
Net annual difference \$ M	-\$47	-\$147	-\$168	-\$179	-\$206
Cumulative difference \$ M	-\$47	-\$194	-\$362	-\$541	-\$746

These suggested reductions are extreme, punitive, and irresponsible in nature. Arguing for a cumulative revenue requirement reduction of a staggering \$746M over the 5 year term is unprecedented even in past periods where intervenors were focused primarily on rate increases in the face of the deteriorating economic climate or when concerns were focused upon total bill impacts greater than inflation.

The Board recognized in the RRFE that some distributors will have significantly large multi-year or highly variable investment commitments that exceed historical levels. The Board therefore created an option for those distributors to file a five year custom application, as an alternative to the indexing approach under the IRM.

Hydro One chose that custom approach because of its intensive capital investments planned for the next five years. These capital investments have been identified through a vigorous investment planning process, taking into consideration of its customers' needs, its system's needs and its assets' needs. Hydro One believes these investments are non-discretionary, prudent and timely.

The reductions urged by Board staff and intervenors ignore this fact.

To illustrate this point, the table below compares what the revenue requirement would have been if Hydro One had elected to file this rate application using a 4th GIRM

approach plus an incremental capital module, with the most extreme reductions urged. As the Board will see, the revenue requirement using the formulaic approach is much higher than it would be if the most aggressive reductions were adopted by the Board, an astonishing \$378M over the test years.

\$ M	2015	2016	2017	2018	2019
4th GIRM with ICM	\$1,415	\$1,441	\$1,481	\$1,523	\$1,563
Intervenor Proposal - Most punitive	\$1,369	\$1,376	\$1,410	\$1,436	\$1,454
Net annual difference %	-3%	-5%	-5%	-6%	-7%
Net annual difference \$ M	-\$47	-\$65	-\$71	-\$87	-\$109
Cumulative difference \$ M	-\$47	-\$112	-\$183	-\$270	-\$378

The fundamental purpose of the Custom IR method of rate-setting is to allow for additional recovery associated with the increased level of work program carried out by the distributor, compared to what would be allowed under a 4th GIRM.

As illustrated above, the extreme reductions urged by intervenors will lead, in some cases, to revenue requirement below what would be allowed under the 4th GIRM.

To operate a distribution system at such low levels will have adverse impact on the system reliability, limit the distributor's ability to respond to demand and lead to the deterioration of its financial viability. Delaying the necessary investments will have negative consequences and is inconsistent with the Board's objective of promoting economic efficiency and cost effectiveness within a financially viable industry, which is part of the foundation of the RRFE.

The reductions urged, if accepted, will result in a significantly reduced return on equity. These arguments ignore the long established finding of this Board and other regulators that a fair rate of return is a true cost to the utility. The Supreme Court of Canada has

upheld this fundamental principle of ratemaking. A Board decision that deprives a utility of its appropriate regulated rate of return can negatively impact its credit rating and impact its ability to borrow funds at reasonable rates.

Hydro One urges the Board to reject arguments for arbitrary and irresponsible reductions which ignore embedded savings, ignore the reasons for the increased revenue requirement and ignore the efforts of the company to control its costs.

HYDRO ONE'S CUSTOM FILING, PRODUCTIVITY AND BENCHMARKING

i. Form of Application

The form and content of Hydro One's application has drawn significant time and attention in the oral hearing and in the arguments of Board staff and intervenors alike. The focus has been on pointing out what others view as inconsistencies with or non-compliance with the RRFE.

Hydro One absolutely disagrees. A Custom application is a custom application.

From the outset, Hydro One has been transparent and has taken great care to ensure that Board Staff and intervenors were informed about the Applicant's proposal and that this rate application was being framed as a custom cost of service application. Hydro One presented the application in this manner as this approach was believed to advance the principles and goals of the RRFE, while meeting the capital intensive needs of this utility. This custom approach also allowed the introduction of the rate smoothing proposed. Adherence to the other rate setting methods would have resulted in a significant one-time increase to reflect additions to rate base in 2015, without mitigating that impact for customers. Hydro One's proposal was for the benefit of ratepayers.

The RRFE provides distributors with the flexibility of selecting a rate setting process that is tailored to its needs. For those distributors that select the Custom IR method for rate setting, there is significant room to tailor an application, recognizing that there will be variation from utility to utility, even though the same rate setting approach is followed. This in turn calls upon the Board to customize its decision making to a particular utility, rather than broad, general principles that may apply across the industry, but not necessarily to a particular applicant before it.

Hydro One has called the application a custom cost of service to make it clear that the rates for the 5 year period were derived using a bottom up analysis, consistent with its business planning processes, rather than using a mechanistic approach inherent in the 4th GIRM. Hydro One has provided a five year forecast of its costs, revenues, inflation and productivity, while adhering to the principles and goals of the RRFE.

The Applicant aligned its application with its historical rate applications, modified however to reflect the specific new requirements of the RRFE.

The creation of the Custom IR rate-setting method was a direct acknowledgement that a “one-size-fits-all” approach to rate-making is not appropriate because distributors are different and have different needs.⁶ Yet, Board staff continually reference consistency and comparability between all 3 rate-making methods which Hydro One submits confuses “consistency” with “sameness”.

Some intervenors like SEC for example have gone so far as to argue that the Board should reject the application based on what SEC characterizes as a complete lack of compliance with the RRFE. Hydro One submits that arguments like that are irresponsible, and, actually contrary to the interests of Hydro One’s ratepayers.

⁶ RRFE Report, pg 9

Some arguments suggest that parties are operating under the flawed assumption that a Custom IR application is the same as a Price Cap IR. It is not. An X-factor is not a necessary feature of a Custom IR application.⁷ For the 4th GIRM and Annual IR Index rate-making methods, the RRFE requires that a “price cap index” and an x-factor be adopted. This is not the case for Custom IR.

Hydro One submits that the stretch factor is not a component in the determination of revenue requirement under the Custom IR rate-setting method. Hydro One strongly believes that efficiency and productivity is essential, regardless of which rate-setting method is used. It has therefore built that into its plan that determines the revenue requirement for the test years.

Thus, it was not incumbent on Hydro One as a Custom IR applicant to propose a productivity factor or a stretch factor, contrary to the assertions of others.

Board Staff and other intervenors rely on “Sharing of Benefits” to argue that a “productivity factor” is required in all three rate-setting methods. Hydro One submits that this reference to a productivity factor refers to the Board’s Total Factor Productivity (TFP). Hydro One observes that the Board has set the productivity factor to be used in rate-adjustment formulas to be zero until 2019.⁸

The RRFE clearly provides that when using Custom IR, benefits are to be determined on a case-by-case basis, rather than requiring a stretch factor as in the other methods. In its recent decision in Enbridge Gas Distribution, EB-2012-0459, the Board did not impose a stretch factor. Rather, the Board found that it was appropriate to develop a forecast which includes self-imposed cost reduction assumptions as a means of ensuring

⁷ *Ibid* pg 13

⁸ EB-2010-0379 *Report of the Board: Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario’s Electricity Distributors*, dated November 21, 2013 and corrected December 4, 2013, pg 17

productivity improvements.⁹ Hydro One's proposal on sharing benefits is akin to what was approved by Board in the recent Enbridge case and is set out in Exhibit I-2.02-1 Staff 11.

Board staff reproduced Table 1 from the RRFE with its view on how Hydro One's application aligns with the Custom IR rate setting method. Hydro One disagrees with the Board staff analysis and has produced its own assessment below:

⁹ EB-2012-0459, Board Decision and Reasons dated July 17, 2014, pg 47

		Custom IR	Hydro One Assessment
Setting of Rates			
"Going in" Rates		Determined in multi-year application review	Multi-year application proposed for 5 year rate plan
Form		Custom Index	Custom cost of service with a rate smoothing mechanism proposed
Coverage		Comprehensive (i.e., Capital and OM&A)	Comprehensive proposed
Annual Adjustment Mechanism	Inflation	Distributor-specific rate trend for the plan term to be determined by the Board, informed by: (1) the distributor's forecasts (revenue and costs, inflation, productivity); (2) the Board's inflation and productivity analyses; and (3) benchmarking to assess the reasonableness of the distributor's forecasts	Bottom-up approach to calculating revenue requirement based on Hydro One's forecasts. Inflation is built into cost forecasts, and TFP productivity factor set at 0 by Board until 2019. Cost reductions highlighted and built into cost forecasts. (Exhibit A-19-1) Benchmarking was provided in Exhibit C1-3-2, Attachment 1; Exhibit C1-5-1, Attachment 1 and Exhibit I-2.06-Staff-33. All other expenditures must go through competitive procurement process (evidence of Ms. Frank, Transcript Vol I, pg 33)
	Productivity		
Role of Benchmarking		See above	See above
Sharing of Benefits		Productivity factor	Productivity factor embedded in application; rate smoothing proposal included; commitment to live by plan
		Case-by-case	
Term		Minimum term of 5 years.	5 year term proposed.
Incremental Capital Module		N/A	N/A
Treatment of Unforeseen Events		The Board's policies in relation to the treatment of unforeseen events, as set out in its July 14, 2008 EB-2007-0673 Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors, will continue under all three menu options.	Compliance with Board policy. Hydro One is proposing annual adjustments akin to those in multi-year rate applications. In addition Hydro One is proposing adjustments outside the normal course of business to manage unforeseen events outside management's control while allowing the 5 year plan to continue.
Deferral and Variance		Status quo, plus as needed to track capital spending against plan	No proposal to establish an account to track capital spending against plan. Account not required as past performance demonstrates adherence to plan and no concerns identified. See TCJ1.13
Performance Reporting and Monitoring		A regulatory review may be initiated if a distributor's annual reports show performance outside of the ± 300 basis points earnings dead band or if performance erodes to unacceptable levels.	Additional Off-ramp conditions proposed to reflect industry landscape. Extensive annual reporting proposed, including a outlined in J4.8 and J5.7.

Hydro One submits that its application complies with the Board's requirements for a Custom IR.

As with any new regulatory guideline or process, Hydro One expects and welcomes the Board's feedback and guidance on the form and content of its application, which the Applicant will implement in future applications. Hydro One expects that the Custom IR requirements will evolve and be clarified as more distributors bring forward applications under the RRFE using this rate setting method.

ii. Productivity and Efficiency

Board staff and intervenors were highly critical of Hydro One's application, arguing that productivity and efficiency were for all intents and purposes ignored by Hydro One.

That is incorrect, unfair and completely ignores the evidence.

Some arguments are premised on a flawed assumption that Hydro One faces no pressure to continuously improve productivity and achieve cost savings. As Mr. Struthers testified, that is simply not the case:

I should indicate that I think your assumption was that we didn't have the same pressures as a normal company did with respect to leaning ourselves or keeping ourselves as thin as we can. I am going to suggest that isn't the case. I am going to suggest that the Ministry of Energy is very much a pressure in ensuring that we do lean ourselves. You will have seen the KPMG benchmarking report that was provided, and I also – I am assuming that you are aware of the Premier's Council Review, which is ongoing currently. And, again, it is another benchmarking review of

both Hydro One and OPG. So it would be unfair to say that the companies are not under consistent pressure in order to do the best that they can and to come up with as many structures and strategies to reduce costs.¹⁰

Hydro One submits that the Board should not fall victim to the same flawed assumption.

Hydro One provided a description of the various efforts the company is making to be more efficient, and several of those have quite a challenge to them.¹¹ While it would have been possible to overlay the built-in productivity and resulting savings with a formulaic-type number, Hydro One believes that the approach it took was more appropriate than proposing formulaic numbers.¹² As Ms. Frank explained, Hydro One saw no benefit of doing that. Hydro One's approach was to reduce actual forecast costs, thus lowering the requested revenue requirement, resulting in lower rates.¹³

The Board's own expert, Dr. Kaufmann observed that longer term plans such as five year plan terms strengthen performance incentives and are especially useful in encouraging initiatives that involve up-front costs to achieve long-run efficiency gains.¹⁴

Hydro One has applied for set rates for a 5 year term. It is greatly incented to manage its expenditures, work programs, outcome measures, service quality indicators and embedded productivity and cost efficiency targets. Risk of failing to garner these savings is borne by Hydro One. Under Hydro One's proposal, the customer is

¹⁰ Transcript Vol 3, pg 23

¹¹ Exhibit A-19-1

¹² Transcript Vol 1, pg 30

¹³ Transcript Vol 1, pg 81

¹⁴ PEG, Defining, Measuring and Evaluating the Performance of Ontario Electricity Networks: A Concept Paper Report to the OEB, April 2011, Pages 11-12.

guaranteed the benefit of the savings whether they are realized or not.

Hydro One has presented its productivity/cost efficiency savings in a format that will allow direct comparison of the savings generated by a specific initiative year after year. This will facilitate trending analysis to help determine areas where the efficiency gains are not being realized as they should be or areas that could be investigated for more productivity/cost efficiencies. Hydro One will track and annually report on its productivity savings.

The Board's productivity factor is currently set at zero and will be updated in 2019.¹⁵ Hydro One is delivering tangible productivity improvements at a time when IRM filers are simply expected to maintain status quo productivity.

The forecast productivity savings are stretch targets for the company.¹⁶ They are the outcome of productivity improvements and the easiest and most straightforward way to measure productivity improvement.

While the rate application as filed did not explicitly include an X-factor, Hydro One did disclose all of the underlying productivity targets that would be included in an X-factor calculation. Hydro One's proposal, using 2015 as the rebasing year, includes an X-factor of 0.29%, a fact which Board staff and intervenors have chosen to ignore.

The productivity factor is intended to be the external benchmark which all distributors are expected to achieve, typically measured using estimates of the long-run trend in

¹⁵ In EB-2010-0379 *Report of the Board: Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's Electricity Distributors* (issued November 21, 2013 and corrected on December 4, 2013), p. 17

¹⁶ Exhibit I-1.01-6 VECC 1; Exhibit I-2.02-1 Staff 11; Transcript Vol 1, pg 48; Transcript Vol 3, pgs 17-18

TFP growth for the industry.¹⁷ It is currently set at zero, but the average annual industry TFP from 2002-2012 is actually negative (-0.33%).¹⁸

The Board's expert, Dr. Kaufmann, specifically excluded Hydro One and Toronto Hydro from the benchmarking analysis. As a result, the actual negative TFP trend is probably bigger. When estimated TFP growth is negative, a zero productivity factor is tantamount to a stretch factor.¹⁹

In contrast to industry trend, Hydro One has made considerable efficiency improvements between 2010 and 2013 as evidenced in Table 3 of the *Empirical Research in Support of Incentive Rate-setting: 2013 Benchmarking Update* (July 2014).²⁰ During that time, Hydro One has improved its performance by 10.4%, the highest improvement achieved by any of the LDC's. Hydro One admittedly has further gains to achieve, but its efforts over the historic short term demonstrate the emphasis that the company has put on cost control.

The planned work program over the rate period 2015 to 2019 has Hydro One's planned productivity and efficiency savings embedded within it. Hydro One's efficiency commitments are clear, extensive and fully supported with a plan on how to achieve them.²¹ The company has done its best to quantify those embedded savings, demonstrating its commitment to continued improvements and will track and report its progress and savings achieved.

¹⁷ In EB-2010-0379 *Report of the Board: Rate Setting Parameters and Benchmarking under the Renewed Regulatory Framework for Ontario's Electricity Distributors* (issued November 21, 2013 and corrected on December 4, 2013), p.12

¹⁸ *Ibid*, pg 15

¹⁹ *Ibid*, pg 18

²⁰ Exhibit K1.1, SEC Compendium for Panel 1; Exhibit I-3.03-1 Staff 60.

²¹ Exhibit A-19-1.

iii. Benchmarking

Board staff and intervenors have also criticized Hydro One based on the alleged absence of benchmarking or insufficient benchmarking. To the contrary, Hydro One has participated in numerous benchmarking studies including:

- Mercer Compensation Benchmarking Study²²;
- Operations and Carrier Management²³;
- A report on the benchmarking review of Inergi fees²⁴
- Two customer satisfaction benchmarking reports²⁵
- Utility Vegetation management Benchmark & Industry Intelligence: 2011-2012 Distribution CN Utility Benchmark Survey Analysis Preliminary Report²⁶;
- Ministry of Energy – Assessment of Benchmarking Reports from Hydro One, dated December 7, 2012 by KPMG²⁷;
- Ministry of Energy – Assessment of organizational and Structural Opportunities at Hydro One, dated February 28, 2013 by KPMG²⁸; and
- Hydro One Rate Payer Impact Analysis, dated February 28, 2013 by KPMG.²⁹

Compensation is Hydro One's largest cost input. A compensation benchmarking study was submitted with the application.³⁰ A benchmarking report on Hydro One's outsourcing fees, which comprise approximately 30% of Corporate Common Costs³¹,

²² Exhibit C1-3-2 attachment 1

²³ Exhibit C1-2-10 pgs 16-17; Exhibits I-4.02-1 Staff 34

²⁴ Exhibit I-4.02-1 Staff 63

²⁵ Exhibit I-2.06-11 EP 23

²⁶ Exhibit J3.10

²⁷ Exhibit 1-3.03-9 SEC 31

²⁸ *Ibid*

²⁹ *Ibid*

³⁰ Exhibit C1-3-2, Attachment 1.

³¹ Exhibit C1-5-1, Attachment 1, p.3.

was also provided.³² As Ms. Frank testified, the balance of Hydro One's expenditures must go through a competitive procurement process which ensures market prices.³³ This should provide ample assurance that cost forecasts are reasonable.

All of the benchmark data accounts for a high percentage of Hydro One's total costs.³⁴

Hydro One is also continually being reviewed in detail by government agencies such as the Ministry of Energy in the KPMG benchmarking reports and the Premier's Council Review that has performed a benchmarking review of both Hydro One and OPG. This serves as a further incentive to aggressively seek efficiencies and continuously improve.

This benchmarking evidence was provided despite the challenges Hydro One has faced in conducting useful benchmarking studies. Mr. Struthers, in his testimony, addressed the difficulties in recruiting participants with no guarantee of anonymity and appropriately defining a peer group, benchmarking subject, and agreed upon methodology³⁵, difficulties which significantly undermine the value of benchmarking. This is further evidenced by the fact that the Canadian Electrical Association terminated its participation in benchmarking in 2011.

³² Exhibit I-4.02-1 Staff 63.

³³ Transcript Vol 1 pg 33

³⁴ When all of the compensation costs allocated to distribution, outsourcing fees and materials costs are included, a high percentage of Hydro One's total distribution costs have been benchmarked.

³⁵ Transcript Vol IV, pgs 70-73 and 79-84. In addition, at pgs 19-20 of the EB-2010-0379 Report of the Board, the Board acknowledged the merit of concerns about peer group analysis in its determination that stretch factors would be based on a utility's actual performance against its own predicted costs (i.e. percentage deviation): *"In general, there is a lack of support amongst stakeholders for the use of peer groups and the Board finds the reasons cited compelling. In particular, stakeholders persuasively argued that there are too many variables that can affect distributor costs to be confident in peer group allocations. The Board notes that unit cost comparisons can still be done without pre-defining peer groups."*

In addition to formal benchmarking, there are other tools that provide similar information.

Hydro One's Corporate Scorecard also serves as a mechanism for internal benchmarking. It is reviewed by the Ministry of Energy and Ministry of Finance officials as the part of the business plan. The scorecard is also used to demonstrate continuous improvement, maintaining a commercial culture and delivering results to customers on a year over year basis. This drives the corporate strategy.

The OEB Scorecard also contains targets that can be used for benchmarking purposes such as SAIDI, SAIFI and CAIDI.

Board staff and intervenors ignore that Hydro One's distribution business has no peers against which it can be benchmarked, a factor acknowledged by the Board's own expert, Dr. Kaufmann.

Dr. Kaufmann stated in his slide presentation delivered on January 10, 2013, slide 23: "Unit cost benchmarking to be based on a comparison of each distributor's unit cost (*i.e.* its total distribution cost divided by an index of output quantity) and the average unit cost of distributors in its designated peer group. Currently there are eleven peer groups, plus Hydro One (which has no Ontario peers).³⁶

Further the PEG slide presentation delivered on May 16, 2013, slide 20, states, "Toronto Hydro and Hydro One excluded because statistical tests show they are significantly and

³⁶ EB-2010-0379 PEG Stakeholder Meeting January 10, 2013

materially impacting the industry TFP trend In incentive regulation, industry TFP trend should not be materially impacted by one or two utilities in the industry”.³⁷

Unfortunately, Hydro One does not believe that any further external benchmarking will assist the Board in determining whether costs at Hydro One are reasonable.

There is merit to tracking Hydro One’s year over year performance and improvements which it will continue to do.

Hydro One also believes that there may merit to review its costs and processes by an external, independent Board appointed expert. Should the Board see merit to such a review for its next distribution rate application, Hydro One will fully participate.

Conclusion

Hydro One believes that its rate application for distribution rates for 2015-2019 complies with the intent and spirit of the RRFE Custom IR rate-setting option and provides useful and meaningful evidence that will allow the Board to set just and reasonable distribution rates.

Hydro One does not believe that any further benchmarking studies are useful or appropriate and is concerned by the level of costs and resources required. If the Board were to accept Board staff’s recommendation to require 5 comprehensive benchmarking studies proposed, Hydro One believes that the Board would also need to approve funding for the studies or order the creation of a variance account to track the costs.

It has been Hydro One’s experience that benchmarking studies are costly, challenging to secure participation and ultimately do not yield any meaningful information that the Board could rely upon.

³⁷ EB-2010-0379 - Empirical Research Presentation May 16, 2013

RECOVERY OF HISTORICAL SMART METER COSTS

Prudence

Hydro One is seeking recovery of \$445.1M in smart meter capital costs and \$59.4M in OM&A costs for the period 2009 to 2014.³⁸ These figures are audited figures and reflect the actual, true costs that Hydro One has prudently incurred to December 31, 2013. The 2014 figures are forecasts, but have been included at the request of Board staff.

In its decision in RP-2001-0032 for Enbridge Gas, the Board established the test for prudence. That test is as follows:

- Decisions made by the utility's management should generally be presumed to be prudent unless challenged on reasonable grounds; [emphasis added]
- To be prudent, a decision must have been reasonable under the circumstances that were known or ought to have been known to the utility at the time the decision was made;
- Hindsight should not be used in determining prudence, although consideration of the outcome of the decision may legitimately be used to overcome the presumption of prudence; and
- Prudence must be determined in a retrospective factual inquiry, in that the evidence must be concerned with the time the decision was made and must be based on facts about the element that could or did enter into the decision at the time.

A party challenging the prudence of decisions must raise reasonable grounds to review the prudence of management's decision. If a challenge to prudence is established, then it is up to a utility to demonstrate that the decision was prudent at the time.

³⁸ Transcript Vol III, pgs 6-7

More recently, the issue of prudent utility expenditures was reviewed by the Ontario Court of Appeal in *PWU v. OEB*³⁹. In that case, PWU appealed the decision of this Board to deny Ontario Power Generation (OPG) committed compensation costs as a result of its collective agreements. In allowing the appeal, the appellate court found that the costs were committed costs that had been fixed by collective agreements and could not be altered. It was unreasonable to cut the costs absent evidence of imprudence at the time of bargaining. Relying on market comparisons not available at the time of the collective bargaining was unreasonable.⁴⁰

The prudence of the smart meter costs Hydro One is seeking to recover must be considered by the Board in light of the legal principles outlined above.

Mandatory Smart Meter Program

Hydro One's smart meter work program and associated costs, included those costs for which recovery is sought in this application, are the result of government policy and form part of Hydro One's distribution licence requirements. The costs are not by any means discretionary and are akin to committed costs.

Hydro One, like other distributors, is subject to a licence requirement that all customers be on Time-of-Use (TOU) rates by June 2011. Unlike other distributors however, Hydro One has had to seek an exemption from that licence requirement because the cellular services that are provided by major carriers simply did not and do not allow communications between Hydro One and approximately 150,000 of its customers.

³⁹ *Power Workers Union (Canadian Union of Public Employees, Local 1000) v Ontario (Energy Board)*, 2013 ONCA 359

⁴⁰ That case, and a similar companion case, are set to be heard by the Supreme Court of Canada in December 2014.

During the first period of the exemption, 2011-2012, Hydro One was able to establish communications with 28,000 more of its customers. This was accomplished by installing numerous collectors and repeaters on the communication network. This was done at a high per meter unit cost.

Hydro One then applied for an indefinite exemption from the TOU licence requirement, but was denied. Instead, Hydro One was granted another two year exemption for the 2013-2014 period. The fact that the Board did not grant the indefinite exemption led Hydro One to continue to make costly investments to improve communication. During this time frame, communications were established for another 11,000 customers, again at a very high per meter cost.

2009-2014 Smart Meter Costs: Comparison to Historical Costs and New Challenges

Hydro One submits that the prudence of the costs for 2009-2014 can be readily accepted as the costs are mandatory and are very similar in nature to those incurred between 2006-2008.⁴¹ The prudence of those costs was determined in a previous disposition of smart meter balances in the Combined Smart Meter proceeding EB-2007-0063, and in Hydro One's 2008 and 2010-2011 distribution rate applications for the smart meter costs that were incurred from 2006 – 2008.

During the 2006-2008 period, Hydro One installed meters in the higher density areas of its service territory in order to reach the largest number of customers in an effort to meet the mandated TOU customer conversion target numbers. During the next period of 2009-2014, Hydro One targeted the rural and lower density areas which were, and were always expected to be, at a significantly higher cost.

⁴¹ The costs over both time periods were to install smart meters and enable them to communicate.

Difficulties faced by Hydro One in connecting customers to TOU rates are largely due to its vast service territory, the very low density of its service territory and the communication challenges that it faces in its rural and remote areas based on infrastructure shortcomings by major cellular carriers. Features of Hydro One's challenges in meeting the TOU requirements, challenges that are not faced by other distributors, include:

- Requirement to establish communications with customers over 640,000 square kilometres with a very low customer density;
- During the 2009-2014 period, costs include expenditures for the communication network for 8303 regional collectors and 36,771 repeaters, which required additional efforts to "tune" the network, requiring additional site attendance to adjust antenna settings on thousands of collectors and repeaters until communications with meters could be established;
- Numerous instances where in order to install the necessary collectors, new poles had to be installed to provide the necessary space and new transformers had to be installed in order to provide power;
- The number of complex, more costly meters was greater in the 2009-2014 period than the earlier period of 2006-2008 where the focus was on mostly residential customers and a large number of installations;
- Costs were also incurred to implement enhancements to smart meter network communication system to improve reliability and information security protocols.

It is important to recognize that the nature of the work for the smart meter program during 2009 - 2014 did not change from the 2006 - 2008 period where the prudence of costs was recognized and recovery allowed. Rather, the costs were higher as the deployment of the smart meter solution was concentrated in the rural and remote parts

of the service territory which required more equipment and more labour per meter. Moreover, this latter time period had communication reinforcement requirements for meters installed during the earlier period which was necessary to meet the minimum standards for billing and to improve meter reliability.

Inappropriate "Benchmarking"

Despite urging for arbitrary reductions, Board staff does appropriately acknowledge that Hydro One's costs may be higher given the unique challenges of deploying the smart meters and the AMI communications infrastructure to vast rural and low density areas. Board staff also acknowledged that Hydro One has unique challenges regarding distance, geography and vegetation which affect remote rate reading. This increases costs to Hydro One, costs that are not faced by other utilities.

Mr. Chhelavda testified that Hydro One buys more hardware like collectors, repeaters and transmitters and related items compared to others. Hydro One also has to buy meters with enhanced communication capability to respond to its service territory challenges.⁴²

Despite the unique challenges faced by Hydro One that impacts costs associated with smart meter deployment, Board staff has attempted to justify cost reductions based on inappropriate comparison utilities like Atikokan Hydro, Sioux Lookout Hydro, Chapleau PUC and Algoma Power. This is a good example of how unreliable benchmarking is unhelpful and can be inappropriately relied upon.

Hydro One does not believe those are suitable comparisons, nor can the unit cost information be relied upon for the following reasons:

⁴² Transcript Vol II, pg 164.

- All of the cost figures Board staff relied upon are derived from historic rate applications filed in 2011 and 2012, reflecting costs that were incurred before those filings. Those costs cannot be compared to cost incurred through to 2014 given usual cost escalations. More importantly, the comparison ignores the additional ongoing OM&A costs that continue to be recorded in a variance account, rather than usual operating costs like other utilities. This illustrates a concern with benchmarking, when appropriate normalization is not taken into account to allow meaningful comparisons;
- These utilities have a very different customer base and service territory. Hydro One services roughly 2 customers per square kilometer on average, and as low as 1 customer per square kilometer in its rural territory. The comparator utilities served 4.5, 5, and 600 customers per square kilometer⁴³. It is far more costly to enable communications in very low density service areas due to increased equipment needs, technological challenges including evolving standards, investigations, including trial and error, to implement unique solutions.

It is unfair to compare Hydro One's costs to these utilities. Based on all of these factors, one would reasonably expect that Hydro One's costs would be higher. Simply because they are does not mean that the costs were not prudent.

Capping recovery at \$484 per installed smart meter as Board staff has urged, which reflects an arbitrary 20% premium, is not principled. Similarly, one cannot simply allocate these arbitrary reductions between OM&A and capital as suggested for actual costs.

⁴³ OEB 2013 Yearbook for Electricity Distributors. Note that for Atikokan and Chapleau, the yearbook does not contain information on the rural service territory size. The calculation was done based only on urban territory size. Having reviewed a map of Chapleau, it is likely that their customer density is approximately 100 customers per kilometer.

Hydro One submits that this proposed approach is irresponsible, unreasonable and is contrary to well established rate making principles.

Ambushed in Final Arguments

Hydro One was ambushed in the closing submissions of Board staff, largely supported by intervenors for significant reductions in the actual incurred smart meter costs. The smart meter cost allocation model was discussed, but the prudence of the smart meter costs was never directly challenged.

“Trial by ambush” has long been disallowed in court litigation, a far more adversarial process than administrative tribunal proceedings. Energy regulation in Ontario is intended to be a collaborative process where parties fully participate, on a reciprocal basis, through all steps in the application process.

When significant cost reductions of mandatory programs are challenged, for the first time in final arguments, the integrity of the entire process is undermined.

Hydro One submits that the only basis upon which the Board can disallow the actual, incurred smart meter costs, is if the costs are found to have been imprudently incurred. There is no such evidence. It would, in Hydro One’s submission, be inappropriate to rely on artificial comparisons as evidence of imprudence especially when the prudence of the costs was not canvassed during the many, many opportunities to do so over the course of this lengthy application.

Negative Financial Impact

Hydro One is also very concerned about the negative financial consequences that will flow should the recovery of regulatory assets that have actually been incurred now be

denied retroactively. Disallowing costs incurred on a work program virtually identical to costs previously reviewed, found prudent and approved will adversely affect Hydro One's risk profile, resulting in a credit downgrade. This in turn increases Hydro One's borrowing costs which adversely affects ratepayers.

Hydro One filed its DBRS Credit Rating Report. That report states, in part:

The stable trend assumes that the regulatory regime under the renewed Regulatory Framework will continue to remain reasonable, allowing the company to earn adequate returns and pass through prudently incurred costs on a timely basis...⁴⁴

Conclusion

The smart meter costs for which recovery is sought, are costs actually incurred by the company. The amounts sought are audited amounts. More importantly, the nature of the costs sought is in keeping with those previously approved by the Board (smart meter costs from 2006-2008). The higher cost pressures that Hydro One faces are evident and have been acknowledged by the Board. There is no evidence that these costs were not prudently incurred.

Board staff and intervenors are seeking nothing more than an indirect attempt for the shareholder to see a significant one time reduction in its bottom line. Hydro One asks that the Board reject these unfounded arguments and asks that the disposition of these smart meter costs be approved as requested.

⁴⁴ Exhibit 1-14-1, Attachment 4: DBRS Credit Rating Report, dated April 2014.

HYDRO ONE'S SUBMISSIONS BY ISSUE

1.0 CUSTOM APPLICATION

1.1 To what extent does the application reflect the objectives and approaches described in the RRFE report?

As outlined above, Hydro One believes that its application does reflect the objectives and the approaches that were described in the RRFE report. Hydro One has conducted its business planning process, considering the outcomes outlined in the RRFE: customer focus, operational effectiveness, public policy responsiveness and financial performance. Those outcomes are achieved with the Board's three main policies of planning, measuring performance and rate-setting.

The Board will measure performance with its Scorecard. In addition, Hydro One's performance in delivering this 5 year distribution plan will be measured annually, with its proposed reporting outcomes. There is also significant monitoring and annual reporting with the annual RRR reporting.

Hydro One has filed a 5 year capital plan as required.

This is a custom rate-setting application as contemplated by the Board. Hydro One has called the application a custom cost of service application to avoid misunderstanding about its proposal. The entire plan is a bottom up plan, rather than a mechanistic or formulaic approach. The essential features of the RRFE have been included as explained above.

1.2 Has Hydro One Distribution responded appropriately to all relevant Board directions from previous proceedings, including commitments from prior settlement agreements?

Hydro One believes that it has responded appropriately to all relevant Board directions from prior proceedings, including a commitment that it made in prior settlement agreement.

Some intervenors, SEC and CCC, have questioned whether Hydro One fulfilled a commitment that it made in the EB-2013-0141 Settlement agreement, the 3rd GIRM for 2014 rates, relating to Smart Grid investments and expenditures. In that settlement agreement, approved by the Board, the parties agreed, in part, as follows:

In that custom cost of service application for 2015-2019, Hydro One will present its proposal to the Board on how best to report upon the progress and results of its smart grid program as part of the custom cost of service rate application annual reporting.

Hydro One acknowledges that it did not put forth a formal proposal. Smart grid capabilities are increasingly incorporated in system refurbishments as the normal course of business as required in the RRFE.⁴⁵ Except for some operations expenditures and a few smart grid trials, the investment in smart grid cannot be separately tracked. Hydro One will report on these specific smart grid expenditures. Hydro One will provide forecast and actual expenditures. However, this changed approach to smart grid means that it cannot have the same monitoring on progress and results as initially contemplated.

⁴⁵ RRFE pg 48

Hydro One does not believe that there was any quantitative reporting that it could provide the Board and stakeholders that would be meaningful given smart grid costs are part of its normal business. There are no useful metrics, units or quantification that Hydro One could annually report to the Board that would assist the parties in assessing the value of smart grid expenditures. The value of smart grid cannot be isolated from the usual course of business.

1.3 What actions should the Board require Hydro One Distribution take at or near the end of the 5-year rate term (e.g. rebasing, plan assessment, measurement of customer satisfaction?)

Hydro One submits that no particular actions are required. Hydro One will apply to the Board in the usual course to rebase and set further rates going forward at the end of the 5-year rate term. Hydro One expects the Board will review its performance of 2015-2019 at that time.

1.4 Is the proposed rate-smoothing mechanism appropriate? Given Hydro One's rate smoothing proposal, should the application include any other ratepayer protection measure such as an earnings sharing mechanism?

Hydro One has proposed a rate smoothing mechanism in order to minimize the rate impact in 2015. Without smoothing, there is a large rate increase in 2015 predominantly caused by the significant capital additions that have come into service since Hydro One's distribution rates were last rebased in 2011.

Some intervenors, AMPCO and CME have argued that the smoothing mechanism should be rejected entirely so that there is customer transparency and customers pay rates at the time costs are incurred. The additional carrying costs associated with the smoothing proposal were also cited as reasons for rejecting Hydro One's proposal.

Other intervenors have agreed with the proposal or the proposal in a modified fashion. SEC and CCC for example urge that the proposal be accepted, but that Hydro One be required to inform customers of the true rates and the smoothed rates.

Hydro One submits that its rate smoothing proposal is in the best interest of ratepayers when all factors are considered. The rate base has increased substantially. The work program is increasing of necessity. Hydro One has listened to the voice of its customer and has tried to mitigate against a significant rate increase in 2015 with its proposal. The proposal, while at a cost (\$20M in carrying costs based on the Board prescribed interest rate for deferred costs), also comes at a cost to Hydro One as its true carrying costs are higher.

Hydro One believes that its proposal strikes the appropriate balance. It reflects customer wishes, Board policy on rate mitigation, avoids rate shock in 2015 and still allows the Applicant to recover its necessary revenue requirement.

The rate smoothing proposal protects customers.

Hydro One does not believe that an earnings-sharing mechanism (ESM) as proposed by certain intervenors is required as it and the rate smoothing proposal are mutually exclusive.⁴⁶

Hydro One does not have a history of over-earning in distribution. In fact, the opposite is true. Hydro One distribution has not recovered its allowed rate of return for a few years.⁴⁷ There is no historical concern or basis to impose an ESM.

⁴⁶ Some intervenors also propose an earnings sharing mechanism on top of a stretch factor. The Board has indicated that an earnings sharing mechanism is a stretch factor redundancy: *It is important to note that stretch factors are consumer benefits. They are somewhat analogous to earnings sharing mechanisms, although stretch factors take effect immediately with the application of the formula and are not dependent on the realization of any productivity gains or excess earnings, as would be the case with an earnings sharing mechanism.*

Hydro One considered an ESM, but has chosen the rate smoothing mechanism. Hydro One believes that overall, it provides more ratepayer protection than an ESM, particularly because of the significant increase in 2015.

2.0 OUTCOMES AND INCENTIVES

2.1 Does Hydro One Distribution's Custom Application adequately consider customer feedback and preferences? Have customer feedback and preferences been adequately reflected in the OM&A and capital spending plans?

Hydro One believes that it has considered customer feedback and preferences in the application. This has been reflected throughout, including in its OM&A and capital spending plans. As indicated above, Hydro One's proposal for both OM&A and capital over the 5 year plan is well below the rate of inflation. This is a direct response to concerns of the customer priorities and preferences which are cost/rate and reliability. The plan as proposed is at the lowest cost to customers while maintaining the existing level of reliability as customers were also quite clear that they are not willing to pay more to improve reliability.⁴⁸

2.2 Does Hydro One Distribution's Custom Application promote and incent acceptable outcomes for existing and future customers (including, for example, cost control, system reliability, service quality, bill impacts)?

Hydro One believes that its application does promote and incent acceptable outcomes for both existing and future customers. Customers' primary concerns are costs and reliability, but not increased costs to improve reliability. The application reflects an

⁴⁷ See Exhibit I-6.03-6, VECC 76. Hydro One provided information to show that it has not earned its allowed rate of return in distribution from 2010-2013 and is not anticipated to do so in 2014 based on forecast information.

⁴⁸ See evidence on Voice of the Customer: Exhibit A-5-1.

investment plan targeted at maintaining reliability, but striving to keep customer impacts as minimal as possible.

The application has responded to customer concerns and also meets target objectives of public and employee safety, regulatory and legislative compliance, system growth and maintenance.

2.3 Does the Custom Application adequately incorporate and reflect the four outcomes identified in the RRFE Report: customer focus, operational effectiveness, public policy responsiveness and financial performance?

Hydro One believes that its application does adequately incorporate and address the outcomes identified in the RRFE.

Hydro One has filed robust evidence of its costs and revenues forecast over the test year horizon, as well as its detailed investment plan over the same time frame. The investment plan was established with the main focus being the four outcomes outlined in the RRFE: customer focus, operational effectiveness, public policy responsiveness and financial performance. Hydro One submits that this approach is consistent with the description of the Custom IR method to rate setting in the RRFE⁴⁹.

2.4 Is the monitoring and reporting of performance proposed by Hydro One Distribution adequate to demonstrate whether the planned outcomes are achieved?

The format of Hydro One's annual reporting has evolved during the course of the proceeding. Hydro One has agreed that it will report information in accordance with

⁴⁹ Report of the Board – Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach dated October 18, 2012 (RRFE Report), pg 18

Undertaking J4.8 and J5.7. Doing so will provide the Board with a complete and accurate account of the successful implementation of the 2015-2019 Distribution System Plan (DSP) and will document the planning process for each year of the plan.

At the time of annual RRR filing, Hydro One will file the following documentation:

- a scorecard to track the eight outcome measures found in in Exhibit A-4-4 as submitted in TCJ1.16, attached as Appendix A⁵⁰
- documentation to describe the performance measures;
- Distribution Budget Memo that includes distribution work program details on OM&A and capital expenditures, as well as the in-service additions greater than \$1M for the year⁵¹; and
- Report on smart grid as explained in Issue 1.2 above.

Various intervenors have urged further additional annual reporting beyond what is required or what has been proposed. Hydro One disagrees with the additional proposals as the proposals add effort, and accordingly costs, without a clear indication of value (eg asset risk scores as it is part of a new developing tool), are redundant (eg number of customer complaints arising out of rate class review as processes in place) or beyond Hydro One's scope (eg annual reporting to ratepayer representatives as annual report are to the Board who in turn distributes information).

Hydro One is also concerned about the additional resources and costs associated with increased levels of reporting.

⁵⁰ Hydro One notes that Board staff has suggested that Hydro One should also report on annual expenditures (see pg 32 of the Board staff argument). Hydro One does not believe this level of annual reporting is necessary or appropriate. Moreover, this level of annual reporting is counter to the purpose of a 5 year application, which includes the ability of the utility to manage its affairs within the test period. The level of reporting urged is a level of micro-management that Hydro One does not believes is in keeping with a 5 year rate approval process.

⁵¹ Please see J4.8 response.

2.5 Are Hydro One's proposed off-ramps, annual adjustments and annual adjustments outside the normal course of business appropriate?

As part of its custom application, Hydro One proposes to make annual adjustments prior to setting rates to reflect changes to cost of capital and working capital.

Cost of Capital

Most intervenors, SEC, CCC, EP, PWU, SEP and CME were in agreement that this annual update for cost of capital was appropriate as it is in keeping with what Hydro One has done in the past and was recently approved by the Board in Enbridge Gas Distribution's rate case, as well as in the acceptance of the Horizon Utilities settlement agreement.

Board staff submitted that the cost of capital could be updated for 2015 and then maintained for the balance of the proposed rate period. Hydro One disagrees with the Board staff submission.

It has commonly been Hydro One's practice, accepted by the Board, to update its cost of capital parameters before each new rate year. There is no reason to depart from this practice and it is contrary to that which was recently applied by the Board in the Enbridge proceeding. Moreover, the Board has previously stated its preference to have the most recent and relevant data available.⁵²

Moreover, not reflecting changes in the debt rates and return on equity simply would mask the utility's true financial performance, one of the objectives of the RRFE.

⁵² EB-2010-0002, Board Decision with Reasons, pg 50.

Working Capital

Hydro One also proposed an annual adjustment to the working capital. The positions of the other parties were mixed.

Board staff, supported by SEC, argued the adjustment was unnecessary as a reasonable forecast could have been made instead. CME disagreed with the Board staff position advising that it added complexity. EP was in agreement with Hydro One's approach.

Hydro One submits that the adjustment, as proposed, should be allowed with an annual adjustment as proposed. Working capital is the amount required to cover the carrying cost of the energy charges on customers' bills. Energy prices are expected to increase over the test years and distributors should be held neutral for this effect, similar to all other pass through charges that the distributor has no control over. An annual adjustment is therefore appropriate.

Hydro One also observes that this adjustment was included as a result of stakeholder feedback received during its initial stakeholder consultation sessions.

Adjustments Outside the Course of Normal Business

Hydro One proposed adjustments that would allow it to apply to the Board for additional funding if certain events occurred [initially referred to by Hydro One as "re-openers" but amended to "adjustments outside the course of normal business"]. All of the types of events proposed would be entirely outside of Hydro One's control and would all have a material impact on revenue requirement. Hydro One proposed a higher materiality threshold of \$7.5M, for a single unforeseen change, rather than the threshold required by the Board of \$1M (used by the Board in RRFE for z-factors).

Board staff submitted that it was in support of the increased materiality threshold, but the proposed adjustments should be denied. Hydro One disagrees with this selective approach to its proposal.

SEC and CCC support the proposed adjustments, provided that they are accompanied by robust evidence explaining why the event is outside of normal business, outside the company's control and material and the adjustments are symmetrical. This is consistent with Hydro One's proposal. CME supports Hydro One's treatment of these events and the higher materiality threshold.

Off-Ramps

Hydro One, as part of its custom filing, proposed off-ramp scenarios, in addition to those included in the Board report on 3rd Generation Incentive Regulation.⁵³ Those proposed off-ramps would apply and allow Hydro One to apply to the Board for revised rate approvals, on a complete evidentiary record, in the event of significant industry restructuring or material changes to Hydro One's service territory. CCC supported Hydro One's proposal.

Board Staff, SEC, CME and SIA submitted that customization of off-ramp policies is not necessary. Hydro One disagrees and believes they are appropriate and moreover are not encompassed within the off-ramp if financial performance is off by a 300 basis points deadband. Hydro One does not believe it appropriate for significant changes to occur, but then delay its response as it waits for the next year's annual reports.

⁵³ EB-2007-0673 Report of the Board on 3rd Generation Incentive Regulation for Ontario's Electricity Distributors dated July 14, 2008.

Moreover, the uncertainty in the sector landscape serves as further support for these additional proposals.

2.6 Are Hydro One's forecasts (revenue, costs, inflation and productivity) reasonable? Should Hydro One be expected to provide benchmarking evidence as an indicator of reasonableness?

See responses to 3.1, 3.2, 3.3 and 6.6.

2.7 Is Hydro One's proposed annual reporting and stakeholder engagement process appropriate?

Outcome Measures

Hydro One acknowledges there was considerable difficulty in defining outcome metrics⁵⁴ and maintains that over time as the Company, stakeholders and the Board gain more experience with outcome measurement, these measures may be refined.⁵⁵

Hydro One appropriately sought input from stakeholders at stakeholder sessions on appropriate outcomes measures. At that time, little assistance was offered for measures alternative to those proposed. Now, Hydro One has received some input on how its proposed outcomes measure could be improved. Hydro One focused its outcome measures on those areas where significant expenditures were being proposed, historical data was available to provide reliable assessments and those that focused on customer experience and value for money.⁵⁶

⁵⁴ Exhibit A-4-4 pg and Transcript Vol VIII pg 15

⁵⁵ Exhibit A-4-4 pg 17

⁵⁶ Exhibit A-4-4 pg 4-5; Transcript Vol 8, pg 15

It is important to recognize that Hydro One proposed outcome measures that would allow parties to assess how Hydro One was delivering on its plan as proposed in this application.

Board staff and intervenors now have numerous suggestions for outcome measures. Hydro One believes that its outcomes are superior to those suggested by others, particularly where the original proposal focused on customer outcomes. If the Board believes it valuable, Hydro One is prepared to amend its outcome metric of number of poles to report \$ per pole and number of pole top transformer with PCB oil replaced to \$ per pole top transformer with PCB oil replaced.

Otherwise, Hydro one believes it outcomes metrics as proposed are more meaningful than the suggestions made by Board staff and intervenors.

Several parties commented on the lack of improvement on some targets proposed by Hydro One over the plan period. Hydro One's plan is to maintain performance at existing levels, reflecting customers' preferences.

Board staff and some intervenors have focused on the concept of "consequences". Hydro One does not believe that consequences are appropriate. Consequences are not provided for in the RRFE. Hydro One has committed to live by the 5 year plan it has proposed. Should it fail to deliver, Hydro One expects that it will be held to account at its next rate application.

2.8 Should the application provide appropriate incentives for line loss reduction?

Hydro One believes that its plan to address line losses is appropriate. There was no concern raised about this issue by Board staff or by intervenors. Hydro One thus submits that no specific incentives are required.

3.0 PROGRAM AND PROJECT EXPENDITURES

3.1 Are the levels of planned operation, maintenance and administration expenditures for 2015-2019 appropriate, and is the rationale for the planning choices appropriate and adequately explained?

Hydro One believes that the planned operation, maintenance and administration (OM&A) is appropriate. The table below outlines the OM&A that is being requested for 2015-2019.

Category	2013	2014	2015	2016	2017	2018	2019
	Actual	Bridge	Test	Test	Test	Test	Test
Sustaining	335.7	320.4	329.5	374.4	380.1	363.2	358.1
Development	11.1	18.4	15.4	17.7	17.0	17.4	17.8
Operations	22.0	30.4	30.2	34.4	34.8	42.2	41.0
Customer Services	148.6	133.7	117.9	116.3	114.7	113.5	115.4
Common Corporate Costs and Other OM&A	88.8	73.8	66.7	62.5	62.4	62.4	62.3
Property Taxes & Rights Payments	4.4	4.6	4.7	4.9	5.0	5.2	5.4
TOTAL	610.6	581.3	564.3	610.2	614.0	603.9	600.0

Board staff observed that the plans for OM&A “are reasonably controlled over the life of the plan” but felt that the overall increase was 10% as Hydro One relied on a 2% inflation forecast. The latter is correct, but OM&A will not increase 10% over the life of the plan, but rather 3.6% which is well below the rate of inflation.

A large percentage of Hydro One's OM&A is demand work. Approximately 1/3 of the Sustaining OM&A expenditure is related to these demand work activities.⁵⁷ Demand OM&A work requires an immediate or timely response to customer, safety and system needs. This work includes responding to service interruptions, resolving public safety hazards, replacing or repairing failed equipment, responding to customer requests and providing underground cable locating services.⁵⁸

Reductions to proposed OM&A must be viewed with caution. Hydro One has repeatedly stated that "it must be recognized that any reductions applied to the test years spending will have a compounding effect on cost pressures in the future."⁵⁹ This cannot be stressed enough. The work must be completed. Any spending that is cut from this application is not spending that is saved, but simply deferred, and likely at a higher cost.

Most intervenors and Board staff did not discuss or levy any significant criticism on particular work programs, except for Vegetation Management which is discussed below and compensation which is addressed under Issue 4.4.

Vegetation Management represents approximately 45% of the Sustaining OM&A work program. Hydro One's distribution system is one of the largest systems in North America and is predominantly rural.⁶⁰ Hydro One has approximately 102,000 km of distribution rights-of-way, which traverse three forest regions in the Province of Ontario.⁶¹ The program is significant.

⁵⁷ Exhibit C1-2-2 pg 4; J5.6.

⁵⁸ Exhibit C1-2-2 pg 4

⁵⁹ *Ibid* pg 3

⁶⁰ Exhibit A-6-1, pg 1

⁶¹ Exhibit C1-2-2, pg 34

Hydro One is proposing to move to an 8 year clearing cycle, though it has admittedly not yet achieved the level of accomplishment required to sustain an 8 year line clearing cycle to date. As Mr. Brown testified, currently 23% of Hydro One's right-of-ways are backlogged beyond an 8 year vegetation management cycle.⁶²

Hydro One is currently on a 9.5 year clearing cycle. ⁶³ If Hydro One's proposal is accepted, it will be on a sustainable 8 year vegetation management cycle by 2023.⁶⁴

Hydro One believes that an 8 year cycle target is appropriate. It is a reasonable goal that can be achieved and will provide benefit to the life-cycle cost and improve system reliability. As Mr. Brown testified, shorter forestry cycles not only have reliability benefits, but also life cycle cost benefits. Those benefits will not be realized however until an entire 8 year cycle is achieved. A lengthier cycle or deferring the cycle and not addressing the backlog as Hydro One has proposed simply results in higher costs when the work is actually completed, impacting reliability as well.⁶⁵

Cycle length is important objective in managing vegetation management costs. Longer cycle lengths lead to inefficiencies as more vegetation mass will accumulate, making clearing work more difficult resulting in higher unit costs. This was clear in the 2009 Benchmarking study which stated, in part:

The length of the cycle is on the fringe of acceptable UVM practice and leads to inefficiencies as a result of excessive vegetation growth between successive maintenance.

⁶² Transcript Vol IV, pg 179

⁶³ J5.10

⁶⁴ Transcript Vol V, pg 21

⁶⁵ Exhibit I-3.01-1 Staff 40

Hydro One's relative efficiency performance has been challenged by a long maintenance cycle that allow for significant amounts of vegetation growth on rights of way and by challenging service territory characteristics. These characteristics include the most rural system of any participating utility in this study and a densely vegetated geography that naturally increases UVM workload.

CNUC expects that if Hydro One is successful in reducing its cycle length in a controlled manner and can sustain accomplishment levels associated with lower cycles, then the company's UVM efficiency will be improved along with system reliability.⁶⁶

While some have questioned the need for moving to an 8 year cycle length now, Hydro One believes that it is the most prudent course of action. The work can be executed if funding is not cut. Given the size of the vegetation management program, any reductions to OM&A are likely to be applied to vegetation management as has happened in the past.⁶⁷

Some arguments commented upon unit costs and increased costs. It is true that unit costs are increasing over the 5 year period as the "backlog of complex areas" is addressed but, once the backlog is clear by 2019 the unit costs return to historic 2012 and 2013 actual levels.⁶⁸ As Mr. Brown explained "...the big driver around the increases to unit costs in this program are really aligned with how much we're having to deal with when we go into these backlogged grids... They're going in there to remove large, heavy branches, ... In many cases, they're having to take trees down

⁶⁶ EB-2009-0096, Exhibit A1-15-2 Attachment 1 pg 4-5. UVM means utility vegetation management. CNUC refers to CN Utility Consulting Inc.

⁶⁷ Exhibit I-3.01-1 Staff 40.

⁶⁸ Exhibit PD1, slide 9

completely. ... those grids are extremely expensive on a kilometer basis. ... So that's what's really driving the increases.”⁶⁹

In addition, one cannot ignore the reality of Hydro One’s service territory. It is expansive, it is difficult terrain and it is remote. Each affects costs. This was recognized in the 2009 Benchmarking study where the consultant stated that “Hydro One has one of the more densely vegetated service territories when measured using the number of trees treated per kilometre and naturally has a greater workload than the average peer utility”⁷⁰. In addition, Hydro One has a best in class safety record, which does come at a higher cost, another fact acknowledged in the Benchmarking study.⁷¹

While the fact of Hydro One’s service territory and associated higher costs is ignored by some, it is similarly unfair to mischaracterize the facts. SEC incorrectly alleges that Hydro One’s costs for vegetation management are twice as high as others utilities. That statement does not normalize for vegetation densities.

Hydro One believes its vegetation management proposal is reasonable and in the best interests of ratepayers.

3.2 Is the level of planned capital expenditures appropriate for the period 2015-2019 and is the rationale for the planning and pacing choices appropriate and adequately explained?

The table below outlines the proposed capital expenditures for 2015-2019 which Hydro One believes are appropriate.

⁶⁹ Transcript Vol V, pg 149

⁷⁰ See reference 66.

⁷¹ See reference 66.

Category	2013	2014	2015	2016	2017	2018	2019
	Actual	Bridge	Test	Test	Test	Test	Test
Sustaining	323.2	286.4	308.2	335.2	359.7	380.4	383.5
Development	192.1	200.2	223.3	206.3	207.7	183.5	199.1
Operations	3.6	5.1	9.4	18.8	7.0	7.0	4.2
Customer Service Capital	6.4	22.9	22.6	9.9	3.9	0.0	0.0
Corporate Common Costs & Other Capital	111.7	109.9	85.4	84.5	83.1	84.2	82.3
TOTAL	637.0	624.5	648.9	654.7	661.4	655.1	669.1

Hydro One's proposal is a 7.1% increase over the 5 year period. This equates to an annual average increase of 1.4% which is well below inflation.

Reductions to the capital program has consequences. Any reductions in the test years will have a compounding effect on cost pressures in the future, and the ability to complete the required work, both in capital replacements and corrective maintenance as well as impact reliability and potentially safety.⁷² As Mr. Brown explained "what we're trying to say is that if we don't have -- if we reduce spending in each of these areas, we're not really saving any money. We're just deferring it to later at a higher cost".⁷³

This fact was recognized by Board staff in its final argument.⁷⁴ Board staff did not recommend any program reductions but did believe that increases in spending called

⁷² Exhibit D1-3-2 pg 4

⁷³ Transcript Vol V pg 39

⁷⁴ Board Staff submissions, pg 45.

into question the business planning process. Hydro One disagrees. Increases now simply reflect deferred spending from prior planning periods.

Despite this fact and negative impact on future ratepayers, many intervenors nonetheless ask the Board to make reductions.

Sustaining capital is increasing significantly over the 5 year plan. It is growing 34% or 6.7% year. Sustaining capital planned over the period represents 53% of the overall capital program on average. The programs which others focused upon include station refurbishments, station transformers and poles. These programs represent, on average, 47% of the sustaining program. Hydro One notes that the ramping up of these programs began previously, as approved in EB-2012-0136, and began at that time in order to avoid an unmanageable backlog.

Station Refurbishments

Hydro One is proposing to increase its station refurbishments to refurbish 194 stations over the 5 year rate period. As Mr. Brown testified, the substation fleet is deteriorating as larger numbers of units approach end of life and are in a deteriorated, high risk condition. Failing to increase the rate of replacement of these units will degrade reliability. This plan will only see 19% of the 27% of high risk stations addressed.⁷⁵

Hydro One proposed increases in spending on station refurbishments in the 2013 IRM application. This application continues that trend. The program is necessary to replace the number of assets that are beyond expected service life (ESL) and in a deteriorating

⁷⁵ Exhibit D2-2-3 ISD #S7.

condition.⁷⁶ Contrary to assertions by SEC, the program is not and never was a “run to fail” plan.⁷⁷

The current rate of planned refurbishments is still insufficient to reduce those assets in operation longer than the ESL.⁷⁸ Hydro One expects that the number of assets in deteriorating conditions will also increase.

Station Transformers

Approximately 24% of the distribution station transformers condition assessments fall into the high risk category. This represents 290 transformers that need replacement in the 5 year period.

AMPCO, supported by SEC, did not take issue with the number of transformer being replaced over the 5 year terms but did question the number of spares purchases planned. The planned spare purchases are outlined in the table below:

Year	2015	2016	2017	2018	2019
Number of Spare Purchases	26	27	26	31	32

Hydro One is proposing to mitigate the risk associated with the transformer asset through a combination of planned station refurbishments and transformer replacements and the sustainment of a spare inventory to address transformers under failing or failed condition. Hydro One will address 156 units through planned replacements over the 2015-2109 period. These planned replacements only address about 54% of the high risk transformers. That leaves another 27 transformer per year that are deemed high risk and prone to major failure that would require a spare transformer replacement. This is

⁷⁶ Exhibit I-3.02-1 Staff 56.

⁷⁷ EB-2012-0136 IR I-2-6.06 PWU 7 part (b).

⁷⁸ Exhibit I-3.02-3 PWU 10 and PWU 6.

in line with the average number of spare purchases Hydro One is proposing in D2-2-3 ISD S-01.⁷⁹

Hydro One submits that risk of transformer failure is mitigated by the spares program.

Poles

Hydro One is proposing to gradually increase its pole replacements from 11,600 poles per year in 2015 to 15,200 poles per year in 2019.

Board staff and intervenors criticized the proposed pace of pole replacements, the ability of Hydro One to complete the planned work and the unit cost of the work.

Hydro One's strategy for the poles program is premised upon both age and condition of the asset, not just age as other have alleged.⁸⁰ 4% of the poles are currently at a high risk which requires replacement over a 5 year term to correct against significant deterioration. The proposed plan from 2015-2019 targets replacement of 66,400 poles which is approximately 4%. This is in line with the number of poles that have been identified as high risk.⁸¹ Moreover, 13% of wood poles are showing defects. Further deterioration will over the 2015-2019 period requiring replacement beyond the current test years.

Currently 11% of poles are > ESL. Assuming the historical replacement rate (average of 11,000 poles per year) is maintained over the 2015 to 2019 it is expected that by 2020 that 18% of poles will be > ESL. Increasing the pole replacement rate to 15,200 poles per year as proposed only reduces this % in 2020 to 17%. The proposed pace only has a very minimal impact on ESL, one factor that informs the pole replacement program.

⁷⁹ Exhibit D2-2-3 ISD S-01.

⁸⁰ Exhibit D1-2-1 pg 20.

⁸¹ J5.9

Hydro One believes that the planned pace of pole replacements is appropriate to address those poles which are both beyond ESL and are deteriorating such that they are a high risk asset which requires replacement over the 5 year horizon.

Intervenors have also questioned Hydro One's ability to complete the planned work. Hydro One disagrees. It has already proven that it they accomplish 10720 replacements in a year. Hydro One is suggesting a gradual ramp up of 600 units in both 2015 and 2016, then a ramp up of 1000 unit per year in the later years of the period until they reach the level of 15,200.⁸² This will allow for a sustainable increase in resources levels required to complete these replacements.⁸³

Hydro One notes that if spending on planned work is cut, that simply exacerbates the potential for more reactive work. As previously explained, a final driver of wood pole replacement work is the impact pole failures have on safety and reliability. When poles fail, they often result in a public safety hazard requiring an emergency pole replacement to restore service. These unplanned repairs are more difficult, take longer and are more costly than a planned pole replacement. The average duration of an unplanned outage involving a pole replacement is nine hours, whereas a planned outage involving a pole replacement is two hours.⁸⁴ Reactive work takes 4 and a ½ times longer to complete.

Hydro One believes that it can deliver its pole replacement program as proposed and that it is a reasonable plan that balances the interests of ratepayers and addressing the needs of those high risk assets.

The arguments by intervenors urging reductions to historic spending levels ignores: the uncontradicted evidence that cuts in spending only defer work, at a higher cost and the

⁸² Exhibit PD1 slide 10

⁸³ Exhibit D2-2-3, S-10

⁸⁴ Exhibit D1-2-1 pg 23.

fact that the needs have been demonstrated and the proposed increases are below the rate of inflation over the entire 5 year planned period of 2015-2019.

3.3 Has Hydro One proposed sufficient, sustainable productivity improvements for the 2015-2019 period, and have those proposals been adequately supported, for example, by benchmarking?

Hydro One believes that its proposals are appropriate. Please see the discussion in the section entitled “Hydro One’s Custom Filing, Productivity and Benchmarking”.

3.4 Is the company’s effort to reduce line losses appropriate?

Board staff had no concern with Hydro One’s proposals relating to line losses. No concerns were raised by intervenors.

Hydro One submits that Hydro One plan to reduce line losses is appropriate and the most efficient manner to address the issue as Mr. Andre testified.⁸⁵

4.0 COMMON COSTS AND PROCESSES SHARED BY HYDRO ONE NETWORKS’ TRANSMISSION AND DISTRIBUTION BUSINESSES

4.1 Are the business planning processes, assumptions and policies used by Hydro One Networks to develop and allocate its distribution and transmission revenue requirement appropriate?

Hydro One’s business planning processes, assumptions and policies are appropriate. Please refer to the additional discussion regarding allocation of common corporate costs and compensation below under Issues 4.2, 4.3 and 4.4.

⁸⁵ See Transcript Volume VII

As in past Hydro One rate proceedings, both distribution and transmission, Hydro One's business planning process was a topic of interest to participants and attracted a good deal of criticism from OEB staff and intervenors alike.

With each successive cost of service rate application, and now this custom cost of service application, Hydro One has provided more and more evidence and explanation about its rigorous business planning process. Hydro One even provided a demonstration of the tools it uses to provide further insight into the process that it undertakes.

Hydro One is proud of its business planning process, and indeed believes that it is an industry leading process. The process is focused upon its work programs and associated risks, balanced against Hydro One's business values and strategic objectives.

Hydro One's business planning process is a bottom up process that begins with identifying what work needs to be done and then is reviewed with the risk associated with different levels of expenditures for the work. The goal is to balance costs with tolerable risks.

The business planning process has been enhanced in recent years with the use of Hydro One's Asset Analytics (AA) tool and Asset Investment Planning (AIP).

While true that different tools or processes may utilize different nomenclature, that does not equate to a conclusion that the entire process is inappropriate or inconsistent, and thus leads to an unreliable, business planning process. To the contrary, the process utilized is objective, attempts to minimize subjective assessments, and endeavours to strike a balance between costs and risks or associated consequences of not performing the work.

It is common sense in many ways. Without any constraints on budgets or an ability to complete work, the risks would be minimized. For example if all wood poles were replaced at once, any risks to reliability, customer service and employee safety associated with the wood pole program could be virtually eliminated. That of course is unrealistic, so the company strives to strike the right balance between the level of work and associated costs on the one hand and the risks that are avoided and those that remain on the other.

Despite Hydro One's efforts to clearly explain and demonstrate the business planning process, Board staff and intervenors remain unclear. Hydro One will attempt to further clarify its process.

Investment Plan Development

The business planning process begins with the development of an investment plan, the investment plan is then prioritized based on risk and then a plan is submitted to the senior management and the Board of Directors for approval.

The development of the investment plan begins with a number of inputs. The inputs are:

- i. determination of customer needs by Hydro One's customer service team through extensive customer satisfaction and transactional research which is communicated to the asset managers and service delivery managed⁸⁶;
- ii. the needs of the assets which are determined based on a multi-dimensional risk-based analysis called an asset risk assessment for all power system assets aided by the using AA tool. The AA tool collects data from various source systems to identify

⁸⁶ Exhibit A-5-1.

six risk factors for various assets based on their values and a composite risk score based on: demographics, condition, economics, criticality, utilization and performance.⁸⁷ Consideration of needs such as added capacity and improved reliability in a specific area and asset renewal where performance is degrading, risk and consequences of a failure are high or safety is at risk are reviewed; and

- iii. the business planning instructions provided which includes: (a) the strategic direction and goals for Hydro One reviewed and established by the CEO and senior management team; (b) the customer load forecast; and (c) the economic outlook including economic statistics, interest rates, labour escalation rates, income tax rates and cost rates for benefits.

Once all of the above inputs are considered, a program level assessment is generated which provides level of risk and associated costs for each work program. Three risk levels are generated. They are unacceptable level of risk, a moderate level of risk or an asset optimal level of risk.

Once the risk based investment levels for each work program are identified, the information is put through to the next step in the process which is the investment prioritization process.

Investment Prioritization Process

The prioritization process converts Hydro One's Distribution business values and key performance indicators into investment criteria and guidelines that are used for managing risk and facilitating trade-offs between all investments. This allows Hydro One to effectively prioritize and pace all investments using a risk based approach that considers customer expectations, asset and business needs within constraints and

⁸⁷ Exhibit A-17-7.

criteria imposed. This process is assisted with the Asset Investment Planning Tool (AIP). This tool incorporates the business values and investment-level decisions across the entire business and generates an investment plan and proposal.

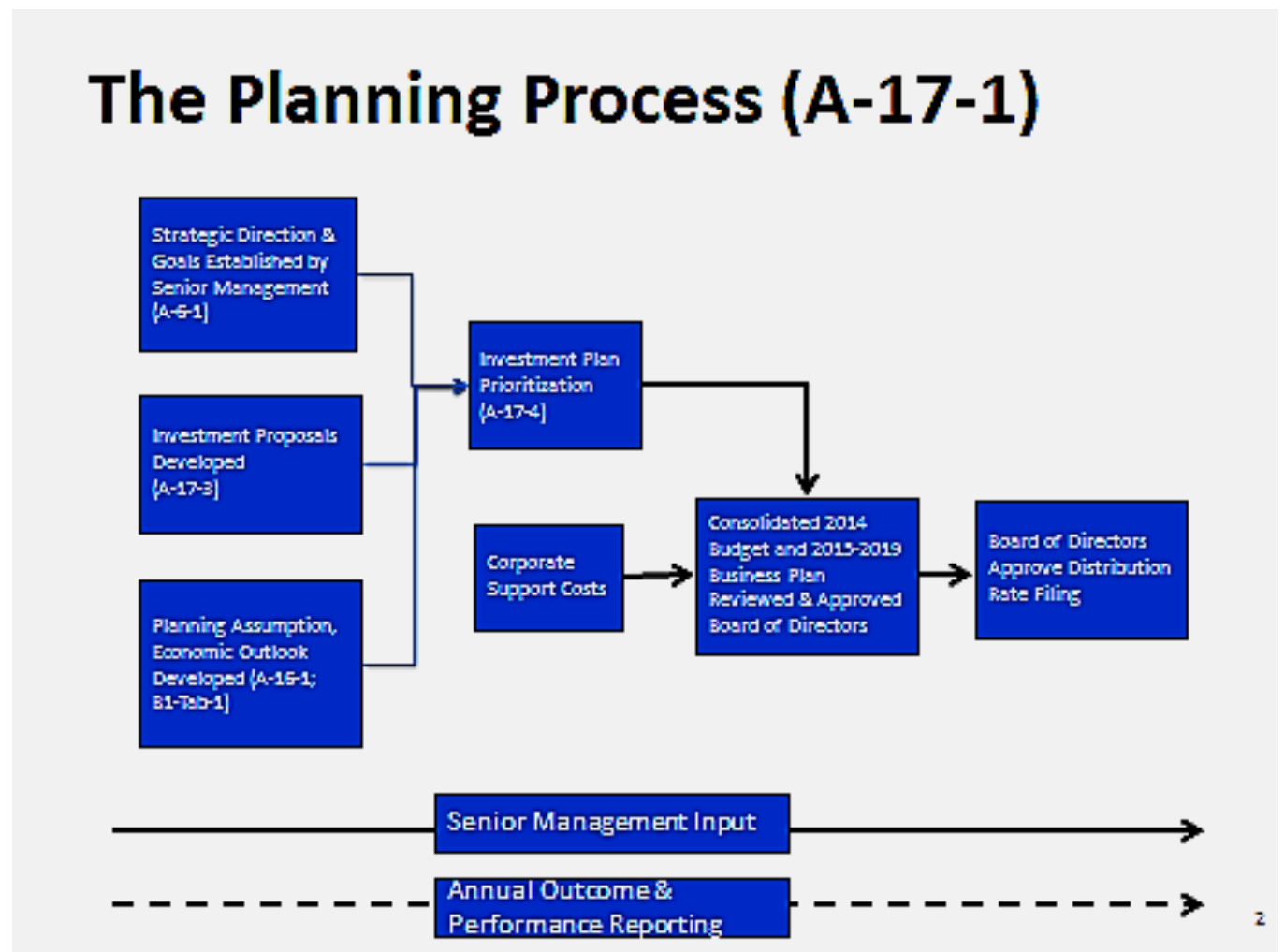
Investment Plan Approval

The investment plan proposal is presented, reviewed and ultimately approved by senior management to finalize the priority and pacing of proposed investments, overheads, common costs and balance customer service levels, rate impacts and economic considerations.

The investment plan is then ultimately approved by the Hydro One Board of Directors.

On-going monitoring and management of work throughput, unit costs and financial spend versus budget is undertaken by the senior operations team on a monthly basis. Issues are identified and addressed.

The steps are shown in the flowchart below.



Intervenors have commented that they would have liked more details regarding some of the many projects and programs.

An extensive list of investment details for each and every investment in excess of \$1M has been provided which includes⁸⁸:

- Priority
- Benefits from maintaining or replacing the asset
- Value for the business and/or customer

⁸⁸ Exhibit I-3.02-1 Staff-52.

- Economics
- Discussion of alternatives
- Impact on rates
- Pacing considerations

Hydro One is unclear on what further details are required from a regulatory approval perspective.

Hydro One believes in its risk based planning process. It continues to make improvements in that process through objective tools to better identify the appropriate work programs. Hydro One's process is an industry leading process, with a proven track record. Hydro One urges the Board to conclude that the process it follows is an appropriate one that both the Board and ratepayers can have confidence in.

4.2 Is the proposed level of 2015-2019 common corporate costs spending appropriate with an adequate demonstration of efficiencies over the 5-year period?

The proposed level of 2015-2019 common corporate costs spending is appropriate with appropriate demonstrated efficiencies. Board staff identified no concerns and no issues were identified by intervenors.

Hydro One requests that the common corporate costs be approved.

4.3 Are the methodologies used to allocate common corporate costs to the distribution and transmission businesses and to determine the overhead capitalization rate for 2015-2019 appropriate?

Hydro One retains external consultants to review cost allocation in support of cost of service type rate applications. There is minimal change, if any, in allocation from year to year. The methodologies are appropriate and were largely not questioned.

One intervenor argued that Hydro One should update the cost allocation report during the term of the 2015-2019 term. Hydro One does not believe it is reasonable or necessary to incur this additional expense given that little change is anticipated. Hydro One will do so at its next rate application.

One area canvassed relates to the accounting for pensions and Other Post-Employment Benefits (OPEBs). Board staff recommended that the Board may wish to initiate a generic proceeding to review accounting for these items. Hydro One agrees with this recommendation.

Hydro One submits that its overhead capitalization rate for 2015-2019 is appropriate. Board staff had no concerns, nor did any of the intervenors. Board staff did argue that the Board should order Hydro One to undertake a capitalization study to compare and contrast principles under each of US Generally Accepted Accounting Principles (US GAAP) and International Financial Reporting Standards (IFRS) accounting.

Hydro One filed a capitalization policy review discussing the different capital policies between USGAAP and IFRS as part of the evidence in this application.⁸⁹ This review compares and contrasts US GAAP and IFRS capitalization principles to highlight where there may be material differences. Hydro One plans to continue reporting under US

⁸⁹ Exhibit C1-5-2, Attachment 2.

GAAP in the foreseeable future due to the significant benefits to ratepayers as the review demonstrates. It is important to recall that the Board approved Hydro One's adoption of US GAAP instead of IFRS because of the significant benefits to ratepayers driven by the overhead capitalization policies under US GAAP.⁹⁰

Given the time and expense associated with doing any study, and even further expense if completed by a third party consultant, Hydro One does not believe that any further study is required.

Board staff also suggested the Board consider changing Hydro One's capitalization rates based on IFRS principles even if the company still files its financial statements to its auditors under US GAAP. That would require Hydro One to maintain two sets of reporting, including OM&A and Capital Expenditures, increasing time and expense. Hydro One does not believe that doing so encourages transparency or regulatory efficiency.

4.4 Is the compensation strategy for 2015-2019 appropriate and does it result in reasonable compensation costs?

Hydro One has repeatedly acknowledged the concerns that the Board and intervenors have expressed about its compensation costs. Hydro One has done the best it can to manage its compensation costs within the significant constraints that it faces.

It is well known that the majority, 90%, of Hydro One's work force is unionized as reflected in collective agreements with PWU, SEP, all of the fifteen Building Trade Unions and the Canadian Union of Skilled Workers.⁹¹

⁹⁰ EB-2011-0268 – Board decision dated November 23, 2011, pg 11

⁹¹ See Exhibit C1-3-2, page 4.

As a result, the challenges that Hydro One faces, as an employer which is legally bound to negotiate collective agreements with highly sophisticated bargaining agents, cannot be ignored. This is particularly so when options available to other unionized employers, like a work stoppage, are not viable or realistic options. The prudence of negotiations is where the focus should be. There is no evidence of imprudent negotiations.

Hydro One is committed to continual improvements in its overall staffing levels and compensation costs. Its strategy includes several components to address its staffing mix, regular employee headcount and overall total compensation costs. These initiatives are explained below.

Unionized Complement and Staffing Mix

It is extremely difficult for Hydro One to drastically alter its union complement over the short term. Hydro One can and will use attrition to, over time, manage and transform its unionized complement. This in turn should reduce overall compensation costs over the longer term.

In addition to transforming its union complement, Hydro One has continued with its efforts to efficiently use staffing mix to reduce overall compensation costs. Hydro One is planning to increase the total proportion of temporary and casual staff that is being hired from 33% in 2013 to 39% in 2019, with an associated 10% increase in the work executed by these lower paid temporary and casual staff.

Hiring Practices and Policies

Hydro One has modified and tightened its hiring practices as part of the overall strategy to reduce total compensation costs. Changes include the current hiring practice

which provides that for every two employees who retire, only one employee is hired⁹² and that CEO approval is required for any additional regular staff.⁹³

Head Count

Hydro One has managed its total regular staff headcount historically and over the business plan period of 2014-2019. That plan demonstrates that while the work program has increased historically and is planned to increase in the future, the regular year end head count historically did not increase in the same proportion, and in fact is expected to decrease by the end of the proposed 5-year rate plan period.⁹⁴

In the period of 2008-2013, the total Networks, both distribution and transmission work program increased by 19.5%, while year-end regular employee count only increased by 10%.⁹⁵

Relevant to this application, the work program forecast over the bridge and test years, for the period 2014-2019, the total Networks, both transmission and distribution, work program is expected to decrease by approximately 4.9%. However, the regular employee count is expected to decrease by 7.5% by year end 2019, a far bigger reduction than the work program.⁹⁶

Bargaining

Hydro One's Human Resources strategy is to negotiate fair and reasonable collective agreements to foster and promote healthy union-management relationships.⁹⁷ It is

⁹² Transcript Volume 3, pg. 48

⁹³ C1-3-1, pg. 5

⁹⁴ Exhibit C1-2-1, pg 5; Exhibit C1-3-2, pg 10; Exhibit C1-3-1.

⁹⁵ Exhibit C1-3-1 pg 5.

⁹⁶ See Exhibit C1-3-2, pg 10

⁹⁷ See Exhibit C1-3-2, pg 4

challenging to achieve wage reductions in bargaining particularly as usual management tools like work stoppages are simply not realistic for Hydro One.

Hydro One has used bargaining to reduce overall compensation. Gains made include modifications to the pension costs. The proportion of pension costs paid by employees increased to 23% in 2013 from a low of 11% in 2010 and will increase even further to 35% in 2019. Hydro One will continue with its efforts to increase employee pension contribution ratio to 50/50 which is the norm for public sector.⁹⁸

Both of Hydro One's primary collective agreements with PWU and SEP are set to expire during the term of the proposed plan. Hydro One has assumed a 2% wage rate increase in the application. That assumption is at Hydro One's risk.

Success in its Strategy

Hydro One's commitment to lowering compensation costs and addressing the concern of Board and intervenors has been proven. Mercer conducted successive Compensation Benchmarking Studies which demonstrate improvement for Hydro One. In 2008 Hydro One was 17% above the market median, 13% above in 2011 and only 10% above in 2013.⁹⁹

Hydro One is making great strides and steady progress in moving closer to market median, even where compared to peers, actively decreasing its own compensation costs.

⁹⁸ See Exhibit I-4.03-1, Staff 68

⁹⁹ See C1-3-2, attachment 1.

As Mr. Struthers testified, the company's goal is to approach the median.¹⁰⁰ It is important to note however, that a median is simply that – some utilities will be above the median and some will of necessity be below.

The substantial improvement was acknowledged by few, and ignored by most. Hydro One submits that its demonstrated history of improvement over a relatively short period of time can be relied upon by the Board when assessing its forecast compensation costs during the proposed 2015-2019 plan.

Hydro One submits that its compensation strategy is sound and reflects reasonable compensation rates.

5.0 DEFERRAL AND VARIANCE ACCOUNTS

5.1 Are the proposed amounts, disposition, discontinuance and continuance of Hydro One's Distribution's existing deferral and variance accounts, as set out in the Custom Application, appropriate?

The proposed amount, disposition, discontinuance and continuance of existing deferral and variance accounts is appropriate. The accounts related to smart meters and smart grid are addressed separately in Issue 5.2 below.

Accounts to be Discontinued

Hydro One Distribution is seeking to discontinue (booking additional principal amounts to the account balances) the following accounts for the 2015-2019 rate period:

- Smart Meter – Minimum Functionality;

¹⁰⁰ See Transcript Vol II, pg 142.

- Smart Meter – Exceeding Minimum Functionality;
- Distribution Generation – Other Costs – HONI - Variance Account;
- Distribution Generation - Express Feeders – HONI - Variance Account;
- Smart Grid Variance Account;
- Distribution System Code (DSC) Exemption Deferral Account;
- Deferred Revenue Project Costs Variance Account (2009); and
- Generator Joint Use Revenue Variance Account.
- Special Purpose Charge Variance Account (1595 - Recovery of Regulatory Balances Account – Sub Account);
- Microfit Connection Charge Variance Account (1508 - Other Regulatory Assets – Sub Account); and
- OEB Cost Differential Account (1508)

No party raised an issue with this aspect of Hydro One's proposal. Hydro One asks that the Board approve discontinuance of all of the accounts listed above.

Disposition of Accounts

The table below reflects the accounts to be cleared:¹⁰¹

¹⁰¹ Exhibit F1-1-3, pg 2, Table 1. Please note that these numbers are as filed and total balance for disposition has changed due to the adjustments to Smart Meter Accounts requested by Board staff.

Description	US of A Account Ref.	Forecast Balance as at Dec. 31, 2014
Retail Service Variance Account	1550 to1588	(36.1)
Rider 9 – Disposition and Recovery of Regulatory Balances (OEB Approved)	1508	(0.7)
Special Purpose Charge Variance Account	1595	0.2
Retail Cost Variance Account	1518 /1548	1.1
Deferred Pension Variance Account	1508	60.1
Microfit Connection Charge Variance Account	1508	(1.6)
Tax Changes Deferral Account (inc HST)	1592	(17.8)
Smart Meter – Variance Account	1555/1556	16.0
Distribution Generation – Other Costs – HONI - Variance Account	1533	(1.2)
Distribution Generation - Express Feeders – HONI - Variance Account	1533	(0.3)
Smart Grid Variance Account	1536	(1.1)
OEB Incremental Assessment Costs	1508	9.3
Distribution System Code (DSC) Exemption Deferral Account	1508	6.7
Deferred Revenue Project Costs Account	2405	(1.8)
Generator Joint Use Revenue Deferral Account	2405	(0.3)
Smart Meter Entity Charge Variance Account	1551	0.7
Total Regulatory Accounts for Disposition		33.2

Hydro One Distribution is requesting that the regulatory account balance of \$33.2M be recovered in a straight-line pattern over the 5 year period 2015-2019 which was not challenged.

Board staff raised an issue with the manner in which Hydro One has been tracking the accounts associated with Renewable Generation Connection and Smart Grid and has asked that they be restated in order to comply with the Accounting Procedures Handbook (APH)

Hydro One disagrees and considers its approach to be more transparent. It is consistent with the Board's methodology of determining revenue requirement, used to set Hydro One's base rates and the revenue requirement calculation in the Board's smart meter model. This methodology takes into consideration the timing of the projects, the cost of capital, depreciation and tax impacts, whereas, the APH does not. The APH does not distinguish between capital expenditures and in-service capital additions which are different concepts.

In addition, the methodology in the APH would only show the cash spent in capital and OM&A, and cash collected through the adders. It does not explicitly show the regulatory asset or liability to be recovered or owed to the rate payers. This leads to discrepancy between financial reporting and regulatory reporting which requires unnecessary reconciliation on USofA reporting.¹⁰²

New Accounts

Hydro One proposed the addition of two new accounts: the Rate Smoothing deferral account and the Bill Impact Mitigation variance account. Board staff and intervenors did not oppose the creation of these accounts. Hydro One asks that they be approved as proposed.

¹⁰² See Exhibit F1-1-1, Attachment 1 and Appendices A and B for further details and information supporting Hydro One's approach.

Board staff argued that the Board should require Hydro One to create an additional new variance account to track the impact on revenue requirement of any in-service capital additions shortfall compared to Board-approved amounts, similar to the account proposed in the settlement for Hydro One Transmission recently in EB-2014-0140.

Hydro One does not believe this proposed account is required. As observed, Hydro One Distribution has been under-earning for the several years and is forecast to under-earn in 2014 as well. In addition, Hydro One Distribution does not have a historical record of below plan in-service capital additions due to the different nature of the work. This is contrary to the transmission business.

Transmission projects tend to take several years to complete. There is a good deal of uncertainty in timing due to the more stringent governmental, environmental and regulatory approval processes, resulting in larger variances in the timing of project in-service dates. On the other hand, distribution projects are much shorter in duration and largely within the company's control.

As discussed, Hydro One's capital plan in this application has been based on the needs and demand identified by the ratepayers and analysis done on the distribution assets through a robust asset risk assessment process and the Asset Analytics tool. Hydro One submitted this five year plan with better information about its system and its customers than ever before, and therefore, does not foresee significant uncertainties in achieving the proposed in service levels.

The rate base will be trued-up based on the actual in-service at the end of the rate term as part of the next cost of service application.

Based on the foregoing, Hydro One does not believe an in-service capital additions variance account is required.

5.2 Is it appropriate to include in rate base, effective January 1, 2015, the following in-service assets which are presently recorded as regulatory assets:

- a) Smart meter assets as of December 31, 2013, the costs for which are recorded in variance accounts 1555 and 1556;**

Hydro One's proposal to recover audited smart meter costs to December 31, 2013 from all metered customers has been fully discussed in the Overview and the written evidence.¹⁰³ In addition, at Board staff's request, Hydro One is proposing to recover forecast smart meter assets to December 31, 2014.

Hydro One proposes to recover the smart meter deferral account balance of \$16.0M from all metered customers, based on the number of customers in each class, which is consistent with the approach used to calculate the Smart Meter Disposition Rider (SMDR) for disposing of the \$6.0M in smart meter costs approved in EB-2007-0681 and the \$16.0M in smart meter costs as approved in EB-2009-0096. In addition, the disposal of the smart meter costs on this basis is consistent with the approach used to set the current \$3.92 Smart Meter Funding Adder (SMFA), which was based on a uniform application to all customers in metered rate classes, regardless of whether the rate class received smart meters. As demonstrated in Attachment 1 of Exhibit G1-5-2, less than \$37,000 is being recovered from the rate classes that did not receive smart meters.

Board staff is critical that Hydro One did not follow the Board's smart meter cost recovery guidelines, instead using its own model that was previously accepted by the Board in EB-2007-0681 as well as the Combined Smart Meter proceeding referenced above. Hydro One does not believe the Board model can accommodate it circumstances, a proposition that Board staff agrees with. Nonetheless Board staff

¹⁰³ Exhibit I-5.02-01 Staff 84.

urges comparison with the Board model and argues for reductions on that basis. Hydro One asks that the Board dismiss any reduction on that basis particularly as the differences between the two are quite minimal.

b) Smart grid assets as of December 31, 2013, the costs for which are recorded in account 1536; and

These assets should be included in rate base effective January 1, 2015 as proposed.

No concern was raised regarding the quantum recorded in the account.

The only issue raised related to the argument made by some intervenors that recovery be denied until Hydro One reported on these investments. Please refer to the discussion on reporting in Issue 1.2 above.

c) Asset to facilitate distributed generation as of December 31, 2013, the costs for which are recorded in account 1533?

These assets should be included in rate base effective January 1, 2015 as proposed.

No issue was taken with the quantum recorded in this account, beyond the comments raised by Board staff regarding APH procedures discussed in Issue 5.1 above.

6.0 REVENUE REQUIREMENT

6.1 Is the rate base component for the revenue requirement for 2015 as set out in the Custom Application appropriate?

Hydro One submits that its rate base component of the revenue requirement for 2015 is appropriate.

The only issues raised about Hydro's One rate base for 2015 related to the inclusion of in service assets that were previously recorded as regulatory assets as discussed in Issue 5.2.

6.2 Is the capital structure and cost of capital component of the revenue requirement for 2015 as set out in the Custom Application appropriate?

Hydro One's capital structure is 60% debt (56% long term and 4% short term) and 40% equity. This is consistent with the Board's reports on cost of capital. No party raised a concern with Hydro One's capital structure.

Hydro One submits that the proposed capital structure is appropriate.

The Applicant has proposed that its cost of capital parameters be adjusted annually, as it has done in previous multi-year cost of service proceedings to update those parameters for each new rate year. Hydro One submits that this is appropriate and ought to be approved. Please review to further discussion in Issue 2.5.

6.3 Is the depreciation component of the revenue requirement for 2015 as set out in the Custom Application appropriate?

Hydro One's depreciation component of the revenue requirement for 2015 is appropriate.

Hydro One reviews the depreciation methodology for each of its cost of service type rate applications. The methodology was reviewed again for this application. The methodology remains consistent with that approved by the Board in 2005.

The only issue relating to depreciation was raised by Board staff who recommended that the depreciation methodology be reviewed at the time of Hydro One's next rate

application. As noted, Hydro One does so in the usual course and expects that it will review the depreciation component again at the time of its next cost of service type application.

6.4 Is the taxes / PILS component of the revenue requirement for 2015 as set out in the Custom Application appropriate?

No issue was taken with the taxes or PILS component of the revenue requirement for 2015 as set out in the Application. Hydro One submits that the taxes/PILS as proposed are appropriate.

6.5 Is the OM&A component of the revenue requirement for 2015 as set out in the Custom Application appropriate?

The OM&A component of the revenue requirement for 2015 is appropriate. Please see discussion in Issue 3.1 above.

6.6 Is the load forecast a reasonable reflection of the energy and demand requirements of the applicant? Is the forecast of other rates and charges appropriate? Is the forecast of other revenues appropriate?

Hydro One has a tried and true load forecast methodology that has a proven track record. Board staff agreed. No significant concerns were identified, though VECC, supported by CCC and EP, did make some comments.

VECC incorrectly characterized Hydro One's load forecast as lacking transparency. Hydro One disagrees with this characterization. Hydro One provided detailed assumptions for all inputs and equations used in the load forecast models.¹⁰⁴

VECC also observed that the final customer and load forecasts were based on judgment. This is correct. In forecasting, judgment is an important and necessary element of reaching the final product, particularly as many inputs and models (econometric and end-use, short-term and long-term, customer survey) are used in determining the final forecast. Since judgment is used, it cannot be definite and precise like a formula.

The reflection of CDM in the load forecast has traditionally been an area of interest for some intervenors, and this hearing is no different. As Mr. But testified, Hydro One believes that it made reasonable CDM forecasts based on the information available to it and the OPA forecasts, a proposition with which Board staff is in agreement.

Hydro One disagrees with VECC's view that the preliminary OPA CDM target savings of 1,200 GWh by 2020 for Hydro One needs to be adjusted in the "Forecasted Savings from Future Programs for 2015-2019" category.

Hydro One notes that the CDM target for Hydro One was only part of a draft report that has not yet been finalized. The category of "Forecasted Savings from Future Programs" has 2 components: (a) program savings funded by the OPA (i.e., CDM target for 2015-2019) and (b) programs initiated by other agencies (Other Influence) such as federal government, provincial government, gas companies, and various associations

¹⁰⁴ See Exhibits A-16-2, A-16-3 and A-16-4. Further information was provided in answers to interrogatories as well. See Exhibit I-1.02-6 VECC 14-25; Exhibit I-6.06-6 VECC 78-89; and Exhibit I-7.02-6 VECC 93-94.

and communities in Ontario. Relying only on OPA funded program savings is not appropriate in Hydro One's view.¹⁰⁵

When the load forecast was updated in April, 2014, the OPA did not have specific estimates. In order to inform how much savings might be attributed to Other Influence for the 2015-2019 period a number of assumptions and calculations are made.¹⁰⁶

¹⁰⁵ See Exhibit A-16-4, page 30, lines 4-6 and Exhibit I- 6.06-6, VECC 87, page 5, where it was explained that the forecasted savings from future programs includes the persistence impacts from Other Influence during 2006-2014 and any other new programs starting in 2015. Counting only CDM target savings is incorrect.

¹⁰⁶ Assumptions and calculations are:

- (i) There are no new Other Influence savings for 2015-2019;
- (ii) Historic Other Influence savings in 2013 of 3 TWh (provided in Exhibit I, Tab 1.02, Schedule 6, VECC 19) will diminish evenly by 15% per year over the 2014-2019 period. That means the persisting savings of Other Influence will be 85%, 70%, 55%, 40%, 25%, and 10% of 3TWh in 2014, 2015, 2016, 2017, 2018 and 2019 respectively. The persistent savings attributed to Other Influence savings for the province are therefore estimated to be 2.55 TWh, 2.1 TWh, 1.65 TWh, 1.2 TWh, 0.75 TWh and 0.3 TWh for 2014, 2015, 2016, 2017, 2018 and 2019 respectively;
- (iii) Assuming 18% share for Hydro One (Exhibit I, Tab 6.06, Schedule 6, VECC 87), the persisting historical savings of Other Influences for Hydro One are estimated to be 459 GWh, 378 GWh, 297 GWh, 216 GWh, 135 GWh, 54 GWh for 2014, 2015, 2016, 2017, 2018 and 2019 respectively;
- (iv) VECC requested the following CDM forecast adjustments in its submission: reduction of 314 GWh in 2015 (1367 GWh – 1681 GWh), reduction of 182 GWh in 2016 (1541 GWh – 1723 GWh), addition of 12 GWh in 2017 (1726 GWh – 1714 GWh), addition of 16 GWh in 2018 (1974 GWh- 1958 GWh) and reduction of 73 GWh (2215 GWh -2288 GWh);
- (v) Estimates of persisting historical Other Influence in 2015-2019 period are compared with the CDM adjustments requested by VECC in the following table:

In GWh	2015	2016	2017	2018	2019
Estimated Persisting Other Influence Savings	378	297	216	135	54
CDM Adjustments requested by VECC	314	182	-12	-16	73

- (vi) Persisting savings from Other Influence are significant and must be considered in the load forecast.

Hydro One does not believe any CDM adjustments in the load forecast are required in light of the foregoing and once the persisting historical Other Influence savings are considered as explained in the footnote.

VECC incorrectly argued that Hydro One did not follow the CDM categories used by the OPA when tracking historical CDM, particularly with the use of Increased Conservation Effects (ICE) in the analysis. Before undertaking the CDM study, Hydro One extensively consulted with intervenors and Board staff on this issue. As directed by the Board, Hydro One worked closely with the OPA in preparing the CDM study. As Mr. But explained, the OPA supported Hydro One's use of ICE in the analysis because these savings are specific to the distribution company.¹⁰⁷

Hydro One has undertaken extensive analysis in tracking the historical CDM by category and had undertaken significant research to estimate the impact of ICE.¹⁰⁸ Hydro One did not include the persisting ICE savings for 2015-2019 as it wanted to be consistent with OPA forecast and the 2013 Long Term Energy Plan in the forecast period. Additionally, if the persisting ICE savings were counted in the forecast years, it would lower the load forecast and add further cost pressure on rates.

Hydro One believes that its detailed CDM analysis is appropriate and disagrees with the criticisms and suggestions by VECC.

The final issue raised with the load forecast relates to Energy Probe's request that Hydro One undertake a price elasticity study during 2015 and adjust the 2016-2019

¹⁰⁷ See Transcript Vol. VI, page 68.

¹⁰⁸ See Exhibit A-16-3.

demand forecast as needed. Hydro One's load forecast has already taken into account the impact of price elasticity in forecasting future demand for electricity.¹⁰⁹

Board staff commented that there is an LRAM mechanism to track the difference between forecast and actual results. This is incorrect. Hydro One does not use an LRAM or LRAM variance account to track any differences and is not proposing to do so.

7.0 COST ALLOCATION AND RATE DESIGN

Hydro One observes that there is no discrete issue that addresses cost allocation, though some submissions were made on this area.

Hydro One has followed the Board's cost allocation model. Hydro One has provided sufficient evidence to ensure the accuracy of the inputs into the model. Most intervenors and Board staff had no issue with the cost allocation methodology, the model inputs or the resulting costs allocated to rate classes. Hydro One does not believe use of the Board model needs to be further justified and explained as SEC has argued. The Board methodology used follows well tested and vetted cost allocation principles and can be accepted by the Board without reservation.

Hydro One submits that the cost allocation methodology is appropriate.

¹⁰⁹ See the annual econometric model at Appendix B in Exhibit A-16-2, pg 28). The annual econometric model used by Hydro One uses electricity price as one of its explanatory variables and the estimated coefficients of this variable is the price elasticity of demand. As Mr. But explained (Transcript Volume 6, pg 166), Hydro One has not done any major studies but has the analysis embedded in the econometric model.

7.1 Are the rate classes and their definitions proposed by Hydro One appropriate?

Hydro One previously had hundreds of rates classes. In EB-2007-0681, Hydro One proposed and the Board accepted an extensive rate class consolidation resulting in 13 different rate classes, including the “Seasonal” rate class.

Subsequently, further review of Hydro One’s rate classification was undertaken. Most recently as part of the EB-2012-0136 IRM proceeding for 2013 distribution rates, Hydro One filed a report of London Economics.¹¹⁰ In that report, London Economics looked at density factors and the cost to serve customers, as well as the appropriateness of Hydro One’s rate classifications. No changes to rate classifications were proposed as a result.

In this application, Hydro One followed that status quo, which had previously been extensively reviewed and approved, except for its proposed modifications to the Seasonal class and the creation of a new “Unmetered Scattered Load” class (USL) as directed by the Board in its Review of Cost Allocation.¹¹¹

There was no issue or concern raised by any party with the creation of the USL class. Hydro One requests that the addition of this rate class be approved as proposed.

The only issue raised regarding rate classification was a concern expressed by SEC. SEC alleged that certain of its customer base, schools, are treated as “rural”. That is incorrect.

Each of the two non-urban general service classes are comprised of a blend of low density and medium density customers. The density factors used to allocate costs to the

¹¹⁰ Customer Density and Customer Service Costs, London Economics International LLC, PowerNex Associates dated November 11, 2011: see EB-2012-0136, Exhibit D-1-1, Attachment 1.

¹¹¹ EB-2010-0219, Review of Electricity Distribution Cost Allocation Policy.

general service classes are akin to the density factors used for medium density customers (like towns), not low density (rural) customers as suggested by SEC.¹¹²

In light of the historical reviews of Hydro One's rate classifications, Hydro One does not believe that any further studies are required. Some degree of cross subsidization between customers within classes is a normal and expected outcome of establishing rate classes (as is evident with other utilities that have a mix of highly urban and rural residential customers), but the concern is not sufficient to warrant committing further resources to once again review the rate classifications.

Hydro One submits that its current rate classes (subject to the comments below on the Seasonal class) and the addition of the USL class are appropriate and ought to be approved by the Board.

7.2 Is the proposed definition of "seasonal" customer class appropriate? Particularly, is residency an appropriate criterion in defining a class? Has this criterion been applied consistently?

The "seasonal" customer class has been an area of interest and concern. Hydro One therefore agreed as part of the settlement reached in its 2013 distribution IRM proceeding to carry out a consultation with interested parties to review the seasonal rate class.¹¹³

Hydro One reviewed the seasonal class and did so, with extensive and appropriate stakeholdering, and proposed an alternative to the status quo that it felt best addressed the concerns that had been identified, and in particular the key concern of high bills for high volume customers.

¹¹² Exhibit G1-3-1 Table 3.

¹¹³ EB-2012-0136, Board Decision and Procedural Order No. 4 dated December 14, 2012.

Hydro One has dedicated an extraordinary amount of time and resources to address this primary concern of high cost, high volume, seasonal customers. This issue was reviewed internally and addressed at several stakeholdering sessions.¹¹⁴ In addition, Hydro One retained an external consultant to conduct focus groups on the issue with interested parties.

Hydro One then considered all of the information, including customer feedback and presented an alternative proposal to address the primary concern. It understood that the proposal was the preferred approach arising out of the focus groups and was consistent with rate making principles.

Despite Hydro One's efforts, there remains no agreement among Board staff and intervenor groups on how best to deal with concerns identified with the seasonal rate class. There are mixed levels of support for Hydro One's proposals or complete opposition.

Hydro One is revenue neutral on this issue, as it is with all matters of cost allocation and rate design. It follows principles of cost causality and fairness when considering appropriate rate classes, allocating costs and setting rates.

Given the complete lack of intervenor support, Hydro One now formally withdraws its proposal for the seasonal rate class and instead requests that the status quo be maintained. Hydro One asks the Board not to implement any changes to the seasonal rate class. This in turn eliminates any concerns with the Rural and Remote Rate Protection (RRRP) issue raised by Board staff and intervenors.

¹¹⁴ See summary in Exhibit I-7.07-10 CCC 29

Board staff identified the status quo as an option for the Board and also suggested that Hydro One further study the issue and again come forward with yet another proposal. Hydro One does not believe any further studies or proposals are warranted. Hydro One committed extensive resources to the process in this proceeding. There is no funding allocated to again review the matter. Given the competing views, Hydro One does not believe there is a proposal that will satisfy the majority of the stakeholders and thus asks that the Board not order it to conduct any further review of the seasonal rate class.

Balsam Lake argued for elimination of the seasonal class. Hydro One does not believe elimination of the seasonal class is appropriate. The seasonal rate class is an appropriate and necessary customer class for Hydro One given its customer base and service territory. The seasonal class reflects principles of cost causality and fairness. The rate class reflects the different consumption and load profiles relative to other year-round residential customers.

The “residency” criterion is part of the definition of a residential customer, year round versus seasonal. The class however was not historically founded upon residency, but rather residency is a simple and reliable proxy for consumption patterns. As explained by Mr. Andre:

-- so -- and I think what the discussion was, that that residency criteria really aligns with -- so what we found is that seasonal customers have that sort of -- a difference load profile and a different consumption pattern, and so, you know, for historical reasons and other we have defined the class based on residency in recognition of the fact that seasonal customers have a distinctly different profile.

So the underlying cost causality principle is that they have a different load profile, a different consumption pattern, and that's why they're recognized as a separate class. The practical way of identifying the customers with that pattern is based on residency criteria.¹¹⁵

Mr. Andre also highlighted that having seasonal customers pay the same rates as year-round residential customers will result in the vast majority of seasonal customers not paying their fair share of the cost to serve them.¹¹⁶

Hydro One submits that the seasonal rate class should remain as it is. If there are future proposals put forward that are supported by stakeholders and in accordance with rate making principles, Hydro One is pleased to consider them.

7.3 Is the reclassification of customers to reflect findings of the company's review of existing customer rate classifications appropriate?

Hydro One undertook a customer rate review and proposed changes to customer rate classifications as a result. The review was intensive and reflects the approved density zone definitions. Hydro One submits that its proposed changes ought to be accepted.

Hydro One observes that no concerns were identified with its rate review, with the process followed for the rate class review or the results that flowed from it.

As part of its proposal, Hydro One committed to undertaking a province wide density review every 5 years and to update density zones to reflect property developments within or adjacent to an existing density zone. Board staff, supported by many

¹¹⁵ Transcript Vol VII, pgs 28-29.

¹¹⁶ Transcript Vol VII, pgs 46-47

intervenors, argued that Hydro One should instead conduct a broader review every 3 years.

Hydro One does not believe that the additional effort and resources required to conduct the in depth review every three year is warranted. While there were a number of changes now, Hydro One does not expect significant changes in the coming years, other than perhaps new subdivisions which it will account for on an ongoing basis, that will materially impact density based rate classifications.

Hydro One believes that its proposal for a province wide review in 5 years, coincidental with its next rate application is appropriate.

Board staff also recommended tracking the number of complaints related to density based classes and the number of reclassifications as a result. Hydro One notes that the complaints are few and it does not believe that the additional costs and resources required to implement this tracking is beneficial. Further, Hydro One believes that this additional tracking mechanism is redundant to Hydro One's proposed ongoing monitoring.

7.4 Is moving revenue-to-cost ratios for all rate classes to within 98% to 102% over the 2015-2019 period appropriate?

Hydro One's proposal to ensure all revenue-to-cost ratios are within Board approved ranges in 2015 is fair and reflects cost causality and is consistent with prior Board direction. Board staff and intervenors were concerned with the impacts of the changes to revenue-to-cost ratios.

Board staff and some intervenors urged that the move to be within the Board approved ranges in 2015 should be phased in.

Hydro One notes that phasing in the 2015 changes to revenue-to-cost ratios may benefit certain ratepayers, but negatively impacts other customers. There is benefit to those who have been underpaying, but not those overpaying as they will continue to do so under a phased in approach.

Hydro One's proposal provides equity between classes and is in keeping with rate making principles.

Some intervenors have asked the Board to widen the band Hydro One proposes as the target for the revenue-to-cost ratios for all classes in 2019. Hydro One believes that the move to the proposed revenue-to-cost ratio band of 98%-102% is appropriate given the significant improvements made to the cost allocation process.

VECC concedes that HONI's use of updated load profiles and incorporation of density factors within the cost allocation model are improvements and Hydro One notes that these are the two most significant factors driving the allocation of costs.

VECC also observed that BC Hydro has a 95% to 105% revenue-to-cost ratio range in part because it has a sophisticated load research analysis. By comparison, the load profiles Hydro One uses are a significant improvement over research used by BC Hydro since they are based on actual load consumption patterns of over 1,000,000 customers. Hydro One's use of its own utility-specific minimum system values in the cost allocation model, based on an independent study previously reviewed and approved by the Board, also represents a significant improvement relative to the allocation based on default values used by other utilities.¹¹⁷

¹¹⁷ Transcript Vol VII pgs 162-164

For these reasons Hydro One believes that its proposal to move to a revenue-to-cost ratio band of 98%-102% at this time remains appropriate. However, Hydro One does accept that adopting a wider band will mitigate rate impacts on certain customer classes, and as such, if the Board believes it is appropriate, Hydro One is agreeable to moving to a band of 95%-105% over the 2016-2019 period covered by this application.

7.5 Is the addition of a new “Unmetered Scattered Load” rate class appropriate?

As outlined in issue 7.1 above, there were no concerns with the addition of the USL class as directed by the Board.

Hydro One submits that this additional rate class is appropriate.

7.6 Are Hydro One’s proposed charges for street lighting appropriate?

No parties, other than the City of Hamilton and VECC, took a position on this issue.

The Board denied Hamilton’s motion to stay this aspect of the application, but did indicate that it would review the issue as part of its main decision.

Hydro One submits that its proposed charges for street lighting are appropriate for the purpose of this application. Akin to other cost allocation issues, the Applicant is revenue neutral. Hydro One does not believe it is appropriate, nor consistent with general regulatory principles, to place the issue of cost allocation on hold simply because there is a pending review.

Contrary to what the City has argued, the rates resulting from the current cost allocation need not apply for the entire 5 year rate period 2015-2019. Should the Board’s cost allocation model be modified and result in changes to the rates for the street

lighting class, Hydro One can implement that change at the time of its annual adjustments.

VECC raised an issue with some traffic lights being included in the street lighting class and asked Hydro One to comment on the practicality of addressing this issue. Hydro One does not believe any changes are required. Of the lights included in the street lighting class, only approximately 1% are traffic lights.

Hydro One does not believe it is at all practical or necessary to remedy this situation. For example, many road intersections are one streetlight “account” for the Ministry of Transportation which includes several street lights as well as a traffic light. The cost to create and maintain separate accounts is not in the interest of ratepayers and would be inefficient. A significant amount of resources and costs would be required to collect the data required for updating the cost allocation model inputs for both the streetlight and USL classes and to carry out the necessary billing system changes and customer communications. This could not be done in less than two years.

7.7 Is an increase to the fixed charges revenue appropriate?

Board staff did not have any concerns with Hydro One’s proposal. While Hydro One’s proposal to increase the fixed charge had some intervenor support, such as by AMPCO, most intervenors were not in favour of the proposed change.

Hydro One believes its approach as proposed is appropriate as it aligned with cost allocation principles underlying the cost allocation model and how those costs are recovered from customers. Hydro One believes that the costs that are driven by the number of customers on cost allocation should be recovered on a per customer basis in rate design

The change proposed is not significant. Hydro One's proposal is to change the fixed charge to recover 42% of revenues compared to the current value of 40%. While the impact on some customer classes is larger than 2%, Hydro One believes that this is demonstrative of the fact that customers in those classes were not paying their fair share of the minimum system costs.

In addition, the current proposal is well below the fixed charges that Hydro One was recovering in the past. The Board and stakeholders will recall that Hydro One proposed, and the Board agreed, to consolidate its rate classes from over 300 to 13. That process was phased in over 4 years as part of the approved rate harmonization plan. Part of that harmonization plan held the quantum of fixed charges flat over the duration of the plan.

In 2008, Hydro One had fixed charges that recovered 48% of revenues as compared to 40% collected in 2014.¹¹⁸ . The subsequent revenue requirement increases from 2008-2011 were absorbed by the volumetric charges.

In addition, Hydro One submits that its proposal is in keeping with the Board direction in its draft report *Rate Design for Electricity Distributors*.¹¹⁹

Some intervenors have argued that the proposal "sacrifices conservation". Hydro One disagrees. Conservation is unlikely to be materially impacted, if at all, by the changes proposed to fixed distribution charges. The distribution component of total bill is typically only 1/3, and fixed charges only a percentage of that, currently 40%. Thus, Hydro One's proposal only impacts 13% of the total bill [33% of total bill x 40% fixed charges].

¹¹⁸ Exhibit G1-4-1, pg 5; Exhibit I-7.07-6 VECC 105 pg 6.

¹¹⁹ EB-2012-0410.

VECC raised an issue with the PLCC (peak load carrying capability) adjustment that is embedded in Sheet O2 of the Board model. This concern is subsumed by Hydro One's proposal for a fixed charge of \$26.57, well below the allocation model calculated amount of \$51.66.

Hydro One believes its proposal is appropriate and further observes that acceptance of the position urged by certain intervenors to maintain the status quo fixed/variable split is extremely problematic for the seasonal rate class. The seasonal fixed/variable split is currently far below what it has been historically and has been maintained artificially low due to the rate harmonization process referenced above. This has been a key contributor to the complaint of high bills from high volume seasonal customers. The fixed revenue share in 2008 for the former R3 and R4 seasonal classes were 63% and 83% respectively.¹²⁰

7.8 Are the proposed charges for miscellaneous services over the 2015-2019 period reasonable?

Hydro One submits that the proposed charges for miscellaneous services are appropriate.

This issue received little attention in this application process.

VECC raised an issue questioning whether Hydro One addressed the joint use charges direction from the Board given in EB-2010-0228. Hydro One did perform a joint use review for space allocation and associated changes and incorporated those changes into the table found at Exhibit G2-5-1.

¹²⁰ I-7.07, Schedule 6, VECC 105, page 6.

SIA raised a concern about the charges for miscellaneous services and in particular that the real cost of providing the services are higher than the fixed rates provided for in the OEB 2006 Rate Handbook. Hydro One agrees that the prescribed charges are far below Hydro One's actual costs.

Hydro One believes its proposal is appropriate as it is in accordance with the Rate Handbook requirements, but also welcomes any review of the 2006 Handbook rates as part of an overall generic process.

7.9 Are the adjustments to reflect the Board-directed line loss study appropriate?

No concerns or comments were received by Board staff or intervenors with respect to the line loss study. Hydro One submits that the adjustments made to reflect the study are appropriate.

7.10 Are the proposed rate mitigation plans appropriate for some customers moving between rate classes in accordance with the results of the rate class review?

This issue only addresses mitigation arising out of the rate class review.

Hydro One believes that its rate mitigation plan for certain customers arising out of the rate class review is appropriate. Customers moving between rate classes as a result of the rate class review will only occur in 2015. That is the year that Hydro One proposed rate mitigation measures.

In subsequent years, Hydro One will address any necessary mitigation at the time rates in 2016 to 2019 are set, in accordance with the Board's guidelines.

While not strictly within the scope of this issue, there is a broader bill impact issue. CCC was the only intervenor who raised this as a concern. Hydro One's proposals have already taken the Board's total bill impact requirements into account. Hydro One has ensured that typical customers have impacts below the 10% total bill permitted by the Board's threshold and has further looked at outliers by examining the bill impacts on high and low volume customers.¹²¹

Hydro One acknowledges that the impacts for Dgen customers and low volume customers in Streetlight, Sentinel Light and USL rate classes are above 10%. However the absolute dollar impacts are small and are below the levels that the Board previously required when considering special mitigation.

EXEMPTION REQUEST - EB-2014-0247

As part of its custom distribution rates application, Hydro One requested a permanent exemption to its distribution licence.¹²² The Board assigned a separate proceeding number to that request, EB-2014-0247. Both proceedings were handled together.

This is Hydro One's final reply argument.

The Distribution System Code (DSC) imposes a service quality requirement, that must be met 100% of the time: a distributor must attempt to contact a customer a missed appointment and attempt to contact the customer within one business day to reschedule the appointment.¹²³

¹²¹ Exhibit G1-7-1 table 1

¹²² Exhibit A-18-1, Appendix A.

¹²³ Distribution System Code, sections 7.5.1 and 7.5.2

Hydro One met 98.4% of all appointments. Of the 1.6% missed, Hydro One only failed to correctly reschedule 12.9% (100% - 87.1%). Hydro One failed to comply with the requirements only 0.2% (1.6% x 12.9%) of all customer appointments.¹²⁴

There is difficulty meeting the requirement. For example, due to unforeseen circumstances such as possible redeployment of staff to respond to an unplanned customer interruption or emergency situation, Hydro One cannot comply with this metric 100% of the time. Other causal factors include Hydro One's vast service territory, areas with not cellular communication and requirements for off road travel.¹²⁵

Hydro One has proposed a permanent exemption so that its target 90%, but does believe that 95% is achievable as Ms. Frank testified.¹²⁶ .

Board staff suggested that any review of the 100% standard is more appropriately done on a generic basis for all distributors.

Hydro One observes that the 2013 OEB Yearbook demonstrated that for "Rescheduling a Missed Appointment":

- 29 LDCs reported 100%
- 4 LDCs reported <100%
- 40 LDCs not reported

The requirement is not met by other utilities, not just Hydro One. Numerous others simply do not report the metric. This supports Board staff comment that a review is more appropriately done on a generic basis. Hydro One agrees.

¹²⁴ Ontario Energy Board, 2013 Yearbook.

¹²⁵ Exhibit I-2.02-2, SIA 10

¹²⁶ Transcript Vol 2, pgs 127-128

Pending any generic review of service quality requirements, Hydro One does require the exemption to ensure that it is in compliance with all of its distribution licence conditions and asks that the Board grant the exemption.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

Appendix "A"

2015	Hydro One Proposed	Board Staff	AMPCO	CCC	CME	SEC	VECC	EP
Stretch Factor (%)		1%	0.6%	1%	2%	-	1%	1%
\$ Impact (\$M)		14.0	-	14.0	28.0		14.0	14.0
OM&A								
Vegetation Management		-	1.9	1.9	1.9	22.8	-	-
Compensation		-	-	15.4	15.4	15.4	-	2.1
Customer Experience		-	3.1	-	-	-	-	-
\$ Impact (\$M)			5.0	17.3	17.3	38.2		2.1
Capital Expenditure								
Pole Replacement		-	8.4	No specific	8.4	6.2	-	17.7
Stations Refurbishment		-	8.5	reduction	8.5	17.3	-	6.9
Transformer Replacement & Spares		-	3.2	amount	-	3.2	-	-
Total			20.1	suggested	16.9	26.7		24.6
\$ Impact (\$M)			1.3		1.1	1.7		1.5
Variance Accounts - Smart Meter								
\$ Impact (\$M)		10.6		10.6				
Total \$ Reduction on Revenue Requirement (\$M)		24.6	6.3	41.9	46.4	39.9	14.0	17.6
2015 Revenue Requirement after Reduction (\$M)	1414.9	1390.3	1408.6	1373.0	1368.5	1375.1	1400.9	1397.3

2016		Hydro One Proposed	Board Staff	AMPCO	CCC	CME	SEC	VECC	EP
Stretch Factor (%)			1%	0.6%	1%	2%	-	1%	1%
\$ Impact			29.4	92.1	29.4	58.8		29.4	29.4
OM&A									
	Vegetation Management	-	24.1	24.1	24.1	14.8	-	-	-
	Compensation	-	3.1	15.4	15.4	15.4	-	-	2.1
	Customer Experience	-	24.1	-	-	-	-	-	-
Total \$ Impact				51.3	39.5	39.5	30.2		2.1
Capital Expenditure									
	Pole Replacement	-	13.2	No specific	13.2	12.6	-	-	19.0
	Stations Refurbishment	-	12.9	reduction	12.9	19.5	-	-	7.8
	Transformer Replacement & Spares		3.7	amount	-	3.7			
	Total		29.8	suggested	26.1	35.8			26.8
Total \$ Impact				3.4		3.0	4.3		3.7
Variance Accounts - Smart Meter									
Total \$ Impact			9.9		9.9				
Total Reduction on Revenue Requirement (\$M)			39.3	146.8	78.8	101.3	34.5	29.4	35.2
2016 Revenue Requirement after Reduction (\$M)		1522.6	1483.3	1375.8	1443.8	1421.3	1488.1	1493.2	1487.4

2017		Hydro One Proposed	Board Staff	AMPCO	CCC	CME	SEC	VECC	EP
Stretch Factor (%)			1%	0.6%	1%	2%	-	1%	1%
\$ Impact			45.2	131.8	45.2	90.4		45.2	45.2
OM&A									
	Vegetation Management		-	26.8	26.8	26.8	17.5	-	-
	Compensation		-	-	15.4	15.4	15.4	-	2.1
	Customer Experience		-	3.1	0.0	-	-	-	-
Total \$ Impact				29.9	42.2	42.2	32.9		2.1
Capital Expenditure									
	Pole Replacement		-	21.5	No specific reduction amount suggested	21.5	22.5	-	21.0
	Stations Refurbishment		-	13.9		13.9	20.0	-	8.0
	Transformer Replacement & Spares			3.1			3.1		
	Total			38.5		35.4	45.6		29.0
Total \$ Impact				6.2		5.5	7.5		6.0
Variance Accounts - Smart Meter									
Total \$ Impact			9.3		9.3				
Total Reduction on Revenue Requirement (\$M)			54.5	167.9	96.7	138.1	40.4	45.2	53.3
2017 Revenue Requirement after Reduction (\$M)		1578.0	1523.5	1410.1	1481.3	1439.9	1537.6	1532.8	1524.7

2018	Hydro One Proposed	Board Staff	AMPCO	CCC	CME	SEC	VECC	EP
Stretch Factor (%)		1%	0.6%	1%	2%	-	1%	1%
\$ Impact		61.3	153.2	61.3	122.6		61.3	61.3
OM&A								
Vegetation Management		-	13.5	13.5	13.5	15.0	-	-
Compensation		-		15.4	15.4	15.4	-	2.1
Customer Experience		-	3.0	0.0	-	-	-	-
Total \$ Impact			16.5	28.9	28.9	30.4		2.1
Capital Expenditure								
Pole Replacement		-	30.0	No specific	30.0	32.7	-	23.0
Stations Refurbishment		-	18.4	reduction	18.4	22.3	-	8.9
Transformer Replacement & Spares			6.3	amount		6.3		
Total			54.7	suggested	48.4	61.3		31.9
Total \$ Impact			9.8		8.8	11.6		8.4
Variance Accounts - Smart Meter								
Total \$ Impact		8.7		8.7				
Total Reduction on Revenue Requirement (\$M)		70.0	179.5	98.9	160.3	42.0	61.3	71.8
2018 Revenue Requirement after Reduction (\$M)	1615.4	1545.4	1435.9	1516.5	1455.1	1573.4	1554.1	1543.6

2019		Hydro One Proposed	Board Staff	AMPCO	CCC	CME	SEC	VECC	EP
Stretch Factor (%)			1%	0.6%	1%	2%	-	1%	1%
\$ Impact			77.9	181.5	77.9	155.8		77.9	77.9
OM&A									
	Vegetation Management	-	6.4	6.4	6.4	6.6	-	-	-
	Compensation	-	-	15.4	15.4	15.4	-	-	2.1
	Customer Experience	-	3.1	0.0	-	-	-	-	-
Total \$ Impact			9.5	21.8	21.8	22.0			2.1
Capital Expenditure									
	Pole Replacement	-	38.9	No specific	38.9	43.3	-	-	25.2
	Stations Refurbishment	-	19.1	reduction	19.1	22.6	-	-	9.0
	Transformer Replacement & Spares		6.8	amount		6.8			
	Total		64.8	suggested	58.0	72.7			34.2
Total \$ Impact			14.4		12.9	16.6			11.1
Variance Accounts - Smart Meter									
Total \$ Impact			8.1		8.1				
Total Reduction on Revenue Requirement (\$M)			86.0	205.4	107.8	190.5	38.6	77.9	91.1
2019 Revenue Requirement after Reduction (\$M)		1659.7	1573.7	1454.3	1551.9	1469.2	1621.1	1581.8	1568.6