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BY COURIER

November 20, 2014

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

EB-2014-0244 - Hydro One Networks Inc. MAAD S86 Application to Purchase Haldimand County Utilities Inc. – Final Argument Submission

In accordance with Procedural Order No. 2, please find attached two (2) paper copies of Hydro One Networks Inc.'s Final Reply Argument related to the MAAD Application for the acquisition of Haldimand County Utilities Inc.

An electronic copy has been filed using the Board's Regulatory Electronic Submission System.

Sincerely,

ORIGINAL SIGNED BY SUSAN FRANK

Susan Frank

IN THE MATTER OF an application made by Hydro One Inc. for leave to purchase all of the issued and outstanding shares of Haldimand County Utilities Inc. under section 86(2)(b) of the *Ontario Energy Board Act, 1998*;

AND IN THE MATTER OF an application by Haldimand County Hydro Inc. seeking to include a rate rider in its 2014 Ontario Energy Board approved rate schedule to give effect to a 1% reduction relative to 2014 base electricity delivery rates (exclusive of rate riders) under section 78 of the *Ontario Energy Board Act, 1998*;

AND IN THE MATTER OF an application by Haldimand County Hydro Inc. for leave to dispose of its distribution system to Hydro One Networks Inc. under section 86(1)(a) of the *Ontario Energy Board Act, 1998*;

AND IN THE MATTER OF an application by Haldimand County Hydro Inc. for leave to transfer its distribution licence and rate order to Hydro One Networks Inc. under section 18 of the *Ontario Energy Board Act, 1998*.

REPLY ARGUMENT OF HYDRO ONE INC. AND HYDRO ONE NETWORKS INC.

INTRODUCTION

In accordance with Procedural Order No. 2, Hydro One Inc. and Hydro One Networks Inc. (hereinafter referred to individually or collectively as “Hydro One”), provide Reply to arguments made by the intervenors, School Energy Coalition (“SEC”), Linda J. Rogers and Board Staff.

HYDRO ONE SUBMISSION

Need for an Oral Hearing and Non-Response or Incomplete Responses to Interrogatories

SEC claims that the Applicants’ responses to interrogatories are “either outright refusals, or non-responsive/incomplete” and that the “Board should make a determination that the record in this proceeding is incomplete, and that an oral hearing is required to test the evidence of the Applicants, and thus complete the record.”¹

¹ EB-2014-0244 – SEC Submission - November 12, 2014 -Page 1

That allegation by SEC is without basis. Hydro One filed this Application using the Board's well-documented, clear requirements set out in the Hydro One Norfolk Power MAAD Decision (EB-2013-0187/EB-2013-0196/EB-2013-0198) as a starting point, which the Board found to be a "...full record. A record that had been developed through a thorough discovery process"². Hydro One took much consideration and thought in responding to interrogatories and has provided full answers to all questions that were within the scope of the hearing. Hydro One also submits that SEC has in no way demonstrated that the Board's choice of process has caused the evidentiary record to somehow be tainted or unreliable for purposes of making an informed decision such that an oral hearing is required.

The Well-Established "No Harm" Test

In its submission, SEC continues to question the meaning of the "No Harm" test. The principles of the "No Harm" test were established in the combined hearing (RP-2005-0018/EB-2005-0234/EB-2005-0254/EB-2005-0257) and further reinforced and thoroughly explored in the matter of Hydro One's acquisition of Norfolk Power Inc. (EB-2013-0187/EB-2013-0196/EB-2013-0198). In the latter Decision, the Board commented that it expected that "its approach in this decision will inform parties contemplating future consolidation transactions"³. The "No Harm" test

"... involves consideration of whether the proposed transaction would have an adverse effect relative to the status quo in relation to the Board's statutory objectives. If the proposed transaction would have a positive or neutral effect on the attainment of the statutory objectives, then the application should be granted. The statutory objectives to be considered are those set out in section 1 of the Act, namely:

1. To protect the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service.
2. To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.
3. To promote electricity conservation and demand management in a manner consistent with the policies of the Government of Ontario, including having regard to the consumer's economic circumstances.
4. To facilitate the implementation of a smart grid in Ontario.

² EB-2013-0187/EB-2013-0196/EB-2013-0198 - Decision and Order on Cost Awards - September 17, 2014
- Page 3

³ EB-2013-0187/EB-2013-0196/EB-2013-0198 - Decision and Order - July 3, 2014 - Page 2

5. To promote the use and generation of electricity from renewable energy sources in a manner consistent with the policies of the Government of Ontario, including the timely expansion or reinforcement of transmission systems and distribution systems to accommodate the connection of renewable energy generation facilities.”⁴

This well-defined test was understood not only by the Applicants but also by Cambridge and North Dumfries Hydro Inc. and Brant County Power Inc. in their MAAD application (EB-2014-0217/EB-2014-0223). The interpretation of the “No Harm” test not only remained unchallenged in that Application but was again applied by the Board in its decision to approve the transaction. Therefore, Hydro One submits that not only is the “No Harm” test clear, but also, contrary to SEC’s assertion, the Board itself has already made clear the components of the test and how they should apply. Hydro One therefore submits that it is unnecessary, unhelpful and inappropriate for the matter to be relitigated in this Application: the record in this Application is complete, and the transaction satisfies the “No Harm” test as defined and established by the Board.

Future Rates in 2020 and Beyond

Both Linda J. Rogers and SEC have questioned the rates that will be charged to HCHI customers after the five-year frozen rate reduction.

As stated clearly in the Application⁵, for the next five years, HCHI customers will have the benefit of a 1% reduction in their base distribution delivery rates, and the resulting reduced rates will be frozen for the entire five-year period. Consequently, these customers will not be subject to **any** increase in base distribution delivery rates that would have resulted through Incentive Rate Mechanism or future cost of service applications.

With respect to HCHI customer rates in year six and beyond, the Board has made it clear that:

“[The] issue of rate harmonization in the context of a consolidation transaction is better examined at the time of rebasing. However, parties should indicate in their application whether they intend to undertake a rate

⁴ EB-2014-0217/EB-2014-0223 – Decision and Order - October 30, 2014 - Page 3

⁵ EB-2014-0244 - Exhibit A, Tab 2, Schedule 1 - Page 11

harmonization process after the proposed transaction is completed and if they do, to provide a description of the plan”⁶.

Hydro One’s application is consistent with Board’s policy on “Rate-Making Associated with Distributor Consolidation”, and as outlined in the prefiled evidence, Hydro One has committed after the rate freeze period to:

“...file a rate application consistent with OEB rate-making principles (e.g. fair, practical, clear, rate stability and effective cost recovery of revenue requirement) in line with the principles noted above. The rate application at that time may propose: (i) to create new acquired customer rate classes; (ii) to move acquired customers to an appropriate Hydro One rate class existing at that time; or (iii) some other option. It is not possible today to say which of these approaches will be adopted as it will depend on the situation at the time of setting the new rates for Hydro One Haldimand. The approach will consider the bill impact on both legacy and acquired customers. Some considerations in deciding on rate strategies include the number and characteristics of the acquired utilities, customer growth in the acquired utilities, and potential development within the electricity regulatory arena in Ontario.

Whichever approach is adopted for setting the rates of acquired utilities, any future proposed rate applications will be subject to OEB approval, satisfy the Board’s “Filing Requirements for Electricity Distribution Rate Applications”, and reflect the actual cost to serve these customers, including the anticipated productivity gains resulting from this consolidation.”⁷

This is consistent with Hydro One’s application and the Board’s Decision and Order in the Hydro One Norfolk Power MAAD Application, wherein the Board wrote:

“Concerning the setting of future rates, it is the Board’s expectation that at the time of rate rebasing HONI will propose rate classes for NPDI customers that reflect costs to serve the NPDI service area, as impacted by the productivity gains due to the consolidation.”⁸

As outlined in Exhibit I, Tab 3, Schedule 9, and Exhibit A, Tab 2, Schedule 1, section 2.0, “HCHI’s future rates will reflect the cost to serve these customers. Therefore,

⁶ EB-2013-0187/EB-2013-0196/EB-2013-0198 - Decision and Order - July 3, 2014 - Page 14

⁷ EB-2014-0244 – Exhibit A, Tab 2, Schedule 1 - Pages 19-20

⁸ EB-2013-187/EB-2013-0196/EB-2013-0198 - Decision and Order - July 3, 2014 - Page 14

ongoing OM&A savings will result in downward pressure on the HCHI ratepayer's cost structure, which would tend to decrease future rates. These savings will be reflected in the lower than status quo OM&A costs, which will be allocated to HCHI ratepayers on then-current cost allocation methodologies"⁹.

Furthermore, it is not feasible to provide a rate impact beginning six years into the future. Rate-setting at the time will be dependent upon a number of factors, including: current and future Board policies (whether rate-making or otherwise); external factors, such as the impact of conservation initiatives on load forecasts; cost of capital; government policy; inflation rates; approval by the Board of any future Hydro One rate design proposals; and the number of acquisitions by Hydro One. To request such information of Hydro One today is a fishing exercise that would be based on speculative information that would not help the Board reach a decision in this Application. Hydro One submits that it is for that reason that it is the Board's policy that rate-setting will be the subject of a future rate application and not dealt with in a MAAD application that took place more than five years earlier.

SEC and Ms. Rogers appear to have ignored Hydro One's evidence that future rate determinations arising from a rate harmonization process have not been determined, nor should such determinations be made at this time. Mere speculation of what the intervenors guess that Hydro One may do in the future is not a reasonable basis for the Board to fairly assess the merits of the Application now before it. Although SEC and Ms. Rogers may be frustrated by not knowing the future, namely, what Hydro One's rate application request may be in a time period more than five years from now, this does not invalidate the relief that Hydro One is seeking. SEC and Ms. Rogers have the option to participate in future rate applications and raise, at such future time, any concerns on proposed rates that they may have.

Contrary Evidence on Costs and Corresponding Rates

SEC has requested that "the Board stipulate, in any decision approving the Applications, that it expects the rate application for HCHI customers in year 6 to result in a reduction in rates and monthly bills for HCHI customers, consistent with the evidence in this proceeding"¹⁰. Hydro One's position is and remains that rate harmonization matters have not been determined and should not be determined in this proceeding. Imposing conditions that predetermine OM&A and capital costs to be used to determine specific customer rates is contrary to the Board's cost-based rate-making principles.

⁹ EB-2014-0244 – Exhibit I, Tab 3, Schedule 9

¹⁰ EB-2014-0244 – SEC Submission – November 12, 2014 – Page 5

Hydro One emphasizes that: (1) MAAD applications do not require Applicants to predetermine future rates; and (2) Hydro One has provided HCHI customers with distribution rates for the next five years, which is consistent with the Board's policies and with the current proposed five-year rate structures for Hydro One Distribution's other customers.

Impact of Transaction on Service Quality and Reliability

Telephone Calls Answered on Time

Regarding SEC's comments on Hydro One's current telephone call response time metrics, Hydro One replied, in response to Exhibit I, Tab 2, Schedule 8, "In 2011 and 2012 we exceeded our target of 80% and, although we have seen a dip in 2013 and likely 2014 due to impacts from replacing our CIS system, we fully expect to return to these high standards in 2015 for all of our customers, including those in Haldimand". Therefore, Hydro One submits that it is improper for SEC to assume that customer service will likely deteriorate for HCHI customers. In fact, as has been reported in the media, Hydro One has recently established a new Customer Advisory Panel to provide independent advice and review to hold the Company accountable for the promises made to its customers.

Scorecard Results – System Reliability

With respect to the SAIDI and SAIFI reliability metrics, SEC has commented that Hydro One (in Table 4 in Exhibit A, Tab 2, Schedule 1), has "cherry-picked data from some of the areas around HCHI, and for only three of the five scorecard years, to 'demonstrate' that Hydro One reliability in the local area is around the same as that of HCHI. Those figures are not from any identifiable source, and have not been tested in any way. In our submission, only the Scorecard figures should be used"¹¹.

Firstly, Hydro One refutes SEC's allegation that Hydro One has cherry-picked data. As described in Exhibit I, Tab 2, Schedule 10, Hydro One provided reliability data that looked at contiguous electrical feeders in geographic locations that serve both Hydro One and HCHI customers. Contrary to SEC's position that Province-wide data should be used, Hydro One submits that the appropriate and relevant data to the customers of Haldimand is reliability data for the geographic area of the transaction, not data gleaned from remote parts of the vast service territory of Hydro One. To clarify any ambiguity, this data is a Haldimand-specific extract of the scorecard results that Hydro One provides to the Board and is tested in the same way that the Provincial scorecard data is tested. Hydro One notes that it is acquiring HCHI staff, facilities and assets, so there is no reason

¹¹ EB-2014-0244 - SEC Submission - November 12, 2014 - Page 6

to conclude that there would be a degradation in the current reliability statistics of the current HCHI. In fact, Hydro One states that reliability measures may even improve over the current measures, due to the elimination of artificial electrical borders.

In response to the concerns expressed by Ms. Rogers regarding comparing reliability between HCHI and Hydro One, Hydro One notes again, as outlined in Exhibit I, Tab 2, Schedule 2, that trying to directly compare a metric, on fundamentally different operating circumstances, is not appropriate. In fact, Hydro One has been identified as an outlier in the Pacific Economics Group April 2007 Report and cannot be compared to other LDCs in the Province, including HCHI, as Hydro One services customers across Ontario (approximately 650,000 km of total service area), many of whom are in hard-to-reach rural and remote areas. The assertion that HCHI customers, once integrated into Hydro One, will receive lower service quality and reliability is flawed. Hydro One has provided evidence that a more appropriate “apples to apples” comparison is to compare statistics in the same geographical area. Hydro One has done this by comparing feeder information in its service area immediately adjacent to Haldimand County with that of HCHI. It makes no sense to compare reliability information that includes data from remote areas, such as in Northern Ontario, to that of areas in southern Ontario, e.g. Haldimand County.

Intervenors have also suggested that the proposed level of capital investments in HCHI will result in a decline in service reliability. Hydro One notes that the Distribution System Plan filed by HCHI was filed on the premise that the organization would continue to operate on a standalone, status-quo basis. That is a fundamentally different operating assumption than what Hydro One intends to achieve going forward with this transaction, namely, fully integrating HCHI’s operational affairs. The proposed level of capital investment reflects Hydro One’s reduced incremental cost to operate and maintain the HCHI service territory. As Hydro One has stated, Hydro One has used an ARA process that considers the state of HCHI’s distribution system, identifies current asset needs, and creates a line of sight to future asset needs. Hydro One has described this process in detail in Exhibit I, Tab 1, Schedule 3. Hydro One’s capital spending forecast for HCHI assets is based upon the same methods it uses for its existing distribution system assets. Hydro One’s existing distribution system and its capital asset programs are well-known and have been used many times at Board hearings to forecast its prospective cost structure. It is both reasonable and appropriate for the expenditure analysis (as shown in Table 2 in Exhibit A, Tab 2, Schedule 1) to be based on these circumstances.

Provincial and Municipal Policy

Ms. Rogers has questioned approval of this transaction based upon current preliminary Provincial energy policy discussions, including the impact of goodwill on potential asset sale transactions. Hydro One submits that such issues are outside of the scope of the “No Harm” test as described above and are also outside the scope of this Application.

As outlined in Exhibit I, Tab 2, Schedule 11, of the Application, Hydro One manages its capital structure to be consistent with the Board’s deemed capital structure of 60% debt and 40% equity, which the Board deems appropriate for all LDCs.

Ms. Rogers also questions the approval process of this transaction and its transparency. Hydro One submits that “selling municipalities are authorized by statute to dispose of their shares in the utility and there are no constraints in the *Electricity Act, 1998*, on their ability to do so”¹². Additionally, as the Board stated in its Decision and Order and Procedural Order No. 8 in the Hydro One Norfolk Power MAAD application, “...the Board also considers that the conduct or motivations of a seller leading up to the consolidation transaction are not relevant to the “no harm” test. The “no harm” test looks at the effect of a transaction, not the reason for or the process preceding the transaction”.

Staff Savings

Ms. Rogers has questioned Hydro One’s ability to place senior HCHI staff into positions within the Hydro One group of companies. As Hydro One stated in its prefiled evidence in EB-2013-0416, Exhibit C1, Tab 3, Schedule 1, much of its existing staff are eligible for retirement and have in fact been retiring. As such, Hydro One does not anticipate having difficulty finding suitable roles for these experienced and knowledgeable HCHI utility staff.

Reporting Requirement

Hydro One agrees with Board Staff’s submission with the exception of Staff’s suggestion that the Board require Hydro One “to file a report with the first rate application that includes costs associated with Haldimand’s service area, delineating the savings achieved as a result of the proposed transaction and how those savings will be allocated.”¹³ Staff suggests that this information would assist the Board in its review of a future rate application. Hydro One submits that Board decisions should help ensure fair, consistent, and equitable treatment of the regulated community. Hydro One notes that the applicants in the Cambridge and North Dumfries Hydro Inc. and Brant County Power Inc. MAAD

¹²EB-2005-0234/EB-2005-0254/EB-2005-0257/EB-2005-0018 - Decision and Order - August 31, 2005-Page 7

¹³ EB-2014-0244 – Board Staff Submission – November 10, 2014 – Page 5-6

application (EB-2014-0217/EB-2014-0223) were not required to file any reports delineating the savings achieved as a result of the proposed transaction. Hydro One submits that a similar and consistent approach as that Application should be taken with the Application before the Board in this proceeding. Hydro One has provided the same, if not greater, detail of where it expects to achieve cost savings and operational efficiencies through the proposed transaction and an outline of expected capital expenditure savings and, as such, submits that there is no justifiable reason for the requested reporting condition.

Hydro One has already indicated that it intends to maintain a separate business unit for the internal management of HCHI's costs. Hydro One will meet all future Board requirements when it applies to harmonize HCHI rates, which will include segment reporting, if required, to support proposed rate-setting methodologies at that time. Hydro One submits that the internal organizational decisions it decides to take to manage its affairs should not become conditions to this Application. Future rates will be the subject-matter of a rate harmonization proceeding, in which costs are anticipated to be examined and potentially presented in evidence.

CONCLUSION

Hydro One therefore submits that the evidentiary record continues to demonstrate that the "No Harm" test is satisfied and that the submissions of the intervenors in this proceeding have not provided any reasonable basis to suggest otherwise. Hydro One respectfully submits that the relief it has requested should therefore be granted.

All of which is respectfully submitted this 20th day of November, 2014.