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BY E-MAIL

April 21, 2017

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto ON M4P 1E4

Dear Ms. Walli:

RE: OEB STAFF SUBMISSION
APPLICATION BY HYDRO ONE INC., ORILLIA POWER DISTRIBUTION CORPORATION, AND HYDRO ONE NETWORKS INC.
EB-2016-0276

In accordance with the OEB's directions, please find attached OEB staff's submission with respect to the above referenced application.

Yours truly,

Original Signed by

Judith Fernandes
Project Advisor
Applications Division

Attachment

cc: All Parties to the Proceeding

ONTARIO ENERGY BOARD

OEB Staff Submission

EB-2016-0276

April 21, 2017

1 INTRODUCTION

Hydro One Inc. (Hydro One) filed an application on October 11, 2016, under section 86(2)(b) of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15 (Schedule B) (the Act), requesting approval to purchase all of the shares of Orillia Power Distribution Corporation (Orillia Power). As part of the share purchase, Orillia Power and Hydro One Networks Inc. (HONI) requested the OEB's approval for related transactions/ proposals:

1. Inclusion of a rate rider in Orillia Power's 2016 OEB approved rate schedule, under section 78 of the Act, to give effect to a 1% reduction in the 2016 base electricity delivery rates for residential and general service classes until 2022
2. Transfer of Orillia Power's rate order to HONI, under section 18 of the Act
3. Transfer of Orillia Power's distribution system to HONI, under section 86(1)(a) of the Act
4. Cancellation of Orillia Power's electricity distribution licence, under section 77(5) of the Act, after the transfer of the distribution system to HONI is completed
5. Amendment of HONI's electricity distribution licence, under section 74 of the Act, at the same time as Orillia Power's licence is cancelled, authorizing HONI to serve Orillia Power's customers

2 RELEVANT REGULATORY PRINCIPLES

2.1 The No Harm Test

In its assessment of applications relating to consolidation transactions, the OEB has applied the no harm test. The no harm test was first established by the OEB in 2005 in the Combined Decision[1], and has been considered in detail in several recent OEB decisions. The *Handbook to Electricity Distributor and Transmitter Consolidation* (Handbook) issued by the OEB on January 19, 2016 confirmed that the OEB will continue to apply the no harm test.

The Handbook states that the OEB considers whether the no harm test is satisfied based on an assessment of the cumulative effect of the transaction on the attainment of its statutory objectives. If the proposed transaction has a positive or neutral effect on the attainment of these objectives, the OEB will approve the application.

The statutory objectives to be considered are those set out in section 1 of the Act:

1 To protect the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service.

1.1 To promote the education of consumers.

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.

4 To facilitate the implementation of a smart grid in Ontario.

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

[1] RP-2005-0018/EB-2005-0234/EB-2005-0254/EB-2005-0257

expansion or reinforcement of transmission systems and distribution systems to accommodate the connection of renewable energy generation facilities.

The OEB recognizes in the Handbook that while it has broad statutory objectives, in applying the no harm test, the OEB has primarily focused its review on impacts of the proposed transaction on price and quality of service to customers, and the cost effectiveness, economic efficiency and the financial viability of the consolidating utilities.

The OEB considers this an appropriate approach, given the performance-based regulatory framework under which regulated entities are required to operate and the OEB's existing performance monitoring framework. There are a number of instruments in place, such as codes and licences, which ensure regulated utilities continue to meet their obligations with respect to the OEB's statutory objectives relating to conservation and demand management, implementation of a smart grid and the use and generation of electricity from renewable resources.

2.2 OEB Policy on Rate-Making Associated with Consolidation

The OEB policies on rate-making associated with consolidation are set out in a report[2] (the 2007 Report) and a further report issued under the same name on March 26, 2015 (the 2015 Report). The Handbook consolidates information provided in these two reports and identifies the key rate-making considerations expected to arise in a consolidation transaction. To encourage consolidations, the OEB has introduced policies that provide consolidating distributors with an opportunity to offset transaction costs with any achieved savings. The 2015 Report permits consolidating distributors to defer rebasing for up to ten years from the closing of the transaction. The 2015 Report also states that consolidating entities deferring rebasing for up to five years may do so under the policies established in the 2007 Report. The extent of the deferred rebasing period is at the option of the distributor and no supporting evidence is required to justify the selection of the deferred

[2] Report of the Board on Rate-making Associated with Distributor Consolidation, July 23, 2007

rebasing period. Consolidating entities, must, however, select a definitive timeframe for the deferred rebasing period.

The rate-setting mechanisms during the deferred rebasing period are clarified in the Handbook. The OEB requires consolidating entities that propose to defer rebasing beyond five years to implement an earnings sharing mechanism (ESM) for the period beyond five years to protect customers and ensure that they share in any increased benefits from consolidation during the deferred rebasing period. The Handbook also confirms that the Incremental Capital Module (ICM), an additional mechanism to allow adjustment to rates for discrete capital projects, is available for distributors that are under the Price Cap IR rate-setting option. Details of the ICM can be found in the OEB reports on new policy options for the funding of capital investments.[3] The ICM is not available for distributors under the Custom IR rate-setting option.

As set out in the Handbook, rate-setting following a consolidation will not be addressed in an application for approval of a consolidation transaction unless there is a rate proposal that is an integral aspect of the consolidation, e.g. a temporary rate reduction. Rate-setting for a consolidated entity will be addressed in a separate rate application, in accordance with the rate setting policies established by the OEB.

[3] OEB Report for the Funding of Capital Investments and OEB Supplemental Report for the Funding of Capital Investments

3 SUBMISSIONS

3.1 The No Harm Test

OEB staff submits that the evidence in this proceeding reasonably demonstrates that the proposed transaction meets the no harm test.

Price, Cost Effectiveness and Economic Efficiency

Hydro One submits that the proposed transaction both benefits and protects ratepayers through: (a) a commitment to freeze base electricity distribution delivery rates for a period of five years from closing of this transaction, (b) the application of a rate rider which provides a 1% reduction on base distribution delivery rates across residential and general service rate classes for that period; and (c) a further sharing of $3.4 million with Orillia Power customers, a result of the guaranteed ESM, in years 11 and forward.

Hydro One projects that the resultant cost structures from proceeding with the transaction will result in ongoing operations, maintenance and administrative (OM&A) savings of approximately $3.9 million per year and reductions in capital expenditures of approximately $0.6 million per year.

Hydro One provides a forecast ten year comparative cost structure analysis for the proposed transaction relative to the status quo, emphasizing that the overall expected savings are based on comparing Orillia Power, remaining as a stand-alone distribution utility, to having Orillia Power's operations becoming integrated with Hydro One's existing operations. Hydro One submits that ongoing OM&A reduction of approximately 60% of Orillia Power's 2015 OM&A costs will result in downward pressure on cost structures relative to the status quo forecast.

According to the application, Hydro One's OM&A forecast to serve customers in its high density residential rate class (UR) is $173 per customer per year as compared to Orillia

Power's cost of $362 per customer per year. Hydro One's urban rate class covers areas containing 3,000 or more customers with a density of at least 60 customers per kilometer. Hydro One submits that as such, it is reasonable to believe that Hydro One will be able to serve Orillia Power's service area, which has about 13,500 customers and a density of 58 customers per km of line, at a cost that is comparable to Hydro One's UR rate class.

Hydro One argues that sustained operational efficiencies are expected to arise from:

a) Elimination of redundant administrative and processing functions in the following areas: financial, regulatory, legal, executive and governance, human resources, and information technology; as well as economies of scale from a larger customer base such that costs for processing systems like billing, customer care, human resources and financial are spread over a larger group of customers
b) Geographic contiguity: Hydro One's existing service area is situated immediately adjacent to Orillia Power's service area which allows for economies of scale to be realized at the field or operational level through more efficient scheduling of operational and maintenance work and dispatching of crews over a larger service area, and more efficient utilization of work equipment (e.g. trucks and other tools), leading to lower capital replacement needs over time and more rational and efficient planning and development of the distribution system

In its application, Hydro One states that it intends to commence construction of a new operations centre within the City of Orillia. In response to interrogatories[4], Hydro One confirms that the need for a new operations centre would still exist even if the proposed transaction was not completed. The new centre consolidates the operations from three separate facilities used by Hydro One as well as the existing Orillia Power facility, which is expected to significantly lower annual operating costs. Hydro One expects to include the costs as well as productivity savings of any operations centre consolidation in its future rate filings as the efficiencies and service improvements will benefit all its customers.

[4] Exhibit 1, Tab 1, Schedule 7, OEB Staff IR#7

Hydro One states that its cost of borrowing is typically lower than that of local LDCs, leading to savings in financing costs over time. The application compares the cost of long-term debt included in Orillia Power's rates of 6.25% with 4.89% as approved in HONI's rates. Hydro One submits that savings that arise from Hydro One's ability to refinance Orillia Power's debt upon maturation at a lower rate will lead to lower debt return on rate base, relative to the status quo.

OEB staff submits that overall, the evidence provided by Hydro One supports the claim that the proposed transaction can reasonably be expected to result in cost savings and operational efficiencies. OEB staff notes, however, that the OEB has set out in the Handbook and in previous decisions[5] that it does not consider a temporary rate decrease to be demonstrative of no harm as it does not reflect underlying cost structures and may not be sustainable or beneficial in the long term.

OEB staff also submits that the operational and cost efficiencies claimed by Hydro One as a result of consolidation may not necessarily translate to lower distribution rates for customers of an acquired entity after the deferred rebasing period has ended. OEB staff observes that the rates proposed for previously acquired utilities (Norfolk, Haldimand, and Woodstock) in HONI's distribution rate application for 2018-2022 (EB-2017-0049) suggests large distribution rate increases for some customers of these acquired utilities once the deferred rebasing period elapses. Despite this observation, OEB staff notes that, in this case, Hydro One has selected a deferred rebasing period of ten years and is committing to a guaranteed sharing of $3.4 million with Orillia Power customers, in years 11 and beyond. As well, the rates that Hydro One proposes for Orillia Power customers after the deferred rebasing period ends and the sharing of efficiency benefits will be subject to OEB review and approval.

OEB staff submits that with respect to Hydro One's proposed construction of a new operations centre, the OEB should, in making its decision, specifically note that it is not

[5] Hydro One Inc./Norfolk PowerDistribution Inc. and Hydro One Inc./Haldimand County Hydro Inc.

approving the construction of this operation centre as part of this proceeding as the OEB will review whether this is a prudent expenditure in a future rate application. In particular, OEB staff would expect that in the future rate application, the OEB would examine the cost/benefit of the new operations centre and whether other options were explored.

Service Quality and Reliability

Hydro One submits that it will endeavour to maintain or improve reliability and quality of electricity service for all of its customers. Hydro One's evidence indicates that it is committed to the retention of Orillia Power's existing operations personnel thereby retaining local knowledge and skills to allow it to maintain or improve reliability and customer service quality.

Hydro One provides a comparison of reliability statistics from 2013-2015 reflecting that Hydro One customers in the vicinity of the City of Orillia experienced a level of service in terms of duration and frequency of interruptions comparable to the level experienced by Orillia Power customers. Hydro One submits that it anticipates that reliability will improve with the combination of pre-existing Hydro One and former Orillia Power resources optimized for the broader Orillia area.

Based on the evidence provided, OEB staff submits that Hydro One can reasonably be expected to maintain the service quality and reliability standards currently provided by Orillia Power.

Financial Viability

Share Acquisition

According to the application, Hydro One will acquire the shares of Orillia Power at a price of $41.3 million, comprised of a cash payment of approximately $26.4 million and the assumption of short and long term debt of approximately $14.9 million. The 2015 net book value of Orillia Power's assets is $22.5 million.

Hydro One states that the premium paid will not be recovered through rates and will not impact any future revenue requirement. Hydro One also states that the proposed transaction will not have a material impact on Hydro One's financial position as the price is less than 1% of HONI's net fixed assets.

Incremental Transaction Costs

Hydro One submits that it expects to incur incremental transaction costs of approximately $3 million for legal, advisory and tax costs relating to completion of the transaction and costs associated with the necessary regulatory approvals. It also expects to incur between $56 million in integration costs, which includes up-front costs to transfer the customers into Hydro One's customer and outage management systems. All of these costs will be financed through productivity gains associated with the transaction and will not be recovered through rates.

In OEB staff's view, the evidence presented by Hydro One regarding the proposed financing of the transaction and the premium paid demonstrates that no adverse impact on Hydro One's financial viability is anticipated.

3.2 Rate-Making Associated With Consolidation

Deferral of Rate Rebasing

Hydro One is choosing to defer the rebasing of rates for Orillia Power's customers for ten years from the date of closing of the proposed share purchase transaction.

Hydro One commits to freeze base electricity distribution delivery rates for a period of five years from closing of the transaction and has requested approval for the application of a rate rider which provides a 1% reduction on base distribution delivery rates across residential and general service rate classes for that period.

From year 6 and up to year 10, Hydro One confirms that rates for Orillia Power customers will be set using the Price Cap adjustment mechanism, as outlined in the OEB's 2015 Report. Hydro One proposed to apply the OEB's Price Cap Index formula utilizing Orillia Power's efficiency cohort factor (0.3%) and this will be anchored to the Orillia Power base distribution delivery rates as approved by the OEB in EB-2015-0024.

OEB staff submits that the deferred rebasing period chosen by the applicants and the proposed rate plan for years 6 to 10 is consistent with the OEB's policies.

Earnings Sharing Mechanism

As set out previously, the 2015 Report requires consolidating distributors who request a deferred rebasing period of greater than five years to implement an ESM.

Hydro One proposes an ESM which guarantees a sharing of $3.4 million of over-earnings with Orillia Power customers. The ESM is calculated on forecast OM&A and capital costs based on comparison of Orillia Power's operations as a stand-alone distribution utility to its expected operations once integrated with Hydro One. The forecast OM&A is about one third of Orillia Power's status quo OM&A forecast, or an approximate 60% reduction in OM&A costs. The OM&A cost forecast includes an adjustment by a 20% risk factor in years 6-10 to compensate for risks assumed by Hydro One in committing to a guaranteed ESM.

The ESM will employ a 50:50 sharing of earnings 300 basis points over Orillia Power's existing approved return on equity. The projected over-earnings amounts to be shared with customers will be recorded in a regulatory account, interest improved, and used to offset future rate mitigation that might be required after the deferral period.

Hydro One submits that the sharing of earnings solely with Orillia Power's customers is consistent with the Handbook, which sets out that a large distributor that acquires a small distributor may demonstrate the objective of consumer protection by proposing an ESM where excess earnings will accrue only to the benefit of the customers of the acquired distributor. Hydro One also submits that the $3.4 million proposed refund is a significant amount, which equates to approximately 45% of Orillia Power's current OEB-approved revenue requirement.

OEB staff submits that the proposed ESM aligns with the expectations of the OEB as set out in the Handbook insofar as applicants can propose an ESM that better achieves the objective of protecting customer interests.

OEB staff notes that Hydro One does not intend to keep separate financial records for Orillia Power; the anticipated reduction in costs is expected to lead to higher synergy savings which is in the best interest of customers. OEB staff also notes that this should be balanced with the expectation for Hydro One to consider savings generated through the consolidation in future rate applications.

OEB staff also submits that Hydro One's commitment to share projected over-earnings, regardless of whether such savings materialize, means that Hydro One will assume certain risks which might otherwise be borne by customers.

Incremental Capital Module (ICM)

Hydro One states that it does not presently plan to apply for ICM relief for Orillia Power during the deferred rebasing period; however, if an ICM were required, the details pertaining to the ICM would be provided in that application.

OEB staff submits that the OEB will consider any ICM request upon the filing of an application. In OEB staff's view though, the ICM would be not be available for investments within HONI's service area because an ICM is not available to distributors setting rates under Custom IR.

Specific Service Charges

Orillia Power requests that its existing rate order, approved in the OEB's Decision and Order EB-2015-0024, be transferred to HONI following the completion of the acquisition transaction. The application states that all of Orillia Power's tariffs will remain as approved by the OEB in its rate order, with the exception of Specific Service Charges for which Orillia Power customers will be charged the Specific Service Charges approved by the OEB for HONI in HONI's rate order EB-2015-0079.

In response to interrogatories[6], Hydro One confirmed that it is seeking approval in this application to amend the Specific Service Charges that would apply to Orillia Power's customers from those currently approved on Orillia Power's Tariff of Rates and

[6] Exhibit 1, Tab 1, Schedule 4, OEB Staff IR#4

Charges to those currently approved on HONI's currently approved Tariff of Rates and Charges, even though no explicit relief has been sought under section 78 of the Act . Hydro One also confirmed that its proposal is not an integral part of the proposed acquisition.

OEB staff submits that Hydro One's proposal to change the Specific Service Charges is not consistent with the Handbook, which states that a change in rates must be an integral aspect of the proposed consolidation for it to be considered in a consolidation application.

The reason given by Hydro One for proposing the changes to the Specific Service Charges is that retaining Orillia Power's existing Specific Service Charges would entail extra work and costs to make these changes to Hydro One's billing system for handling service to Orillia Power's customers. Hydro One argues that many of the Specific Service Charges date back to the *2006 Electricity Distribution Rate Handbook*, issued May 11, 2005.

HONI filed its distribution rate application (EB-2017-0049) on March 31, 2017 in which it confirms completion of a study to update the Specific Service Charges, as directed by the OEB in a previous Decision (EB-2013-0416). As a result of this study, HONI is proposing changes to these charges in its distribution rate application.

OEB staff understands Hydro One's argument relating to additional cost for system changes and for customer handling, but also considers that it may be premature to approve changes given HONI's proposed amendments to Specific Service Charges in its distribution rate application.

OEB staff notes that the changes proposed in this consolidation application are not integral to the consolidation and there is no evidence that Orillia Power's customers were given notice of the proposed changes to the Specific Service Charges.

OEB staff submits that the question for the OEB to consider is whether it should approve Hydro One's proposal for the changes to the Specific Service Charges even though the proposal is not in accordance with the policy in the Handbook or whether Hydro One would have to make a separate application before the OEB or address it in HONI's distribution rate application for all of its customers and service territories.

Rate Riders in Orillia Power's Rate Order

Orillia Power is requesting a rate rider to reduce the residential and general service rate classes' base distribution delivery rates that are effective May 1, 2016 by 1% for years one through five of the deferral period.

OEB staff submits that the OEB has approved in its decisions on previous consolidation applications[7] the applicants' proposals to implement a 1% reduction to each of the acquired utilities' rates in effect at the time and also approved the maintenance of a rate freeze at this level for a five year period from the closing of the transactions. OEB staff supports Orillia Power's requested rate rider.

OEB Staff Interrogatory 4 b) required the applicants to confirm whether any extension or amendment is being sought through this application for rate riders which have an expiry date within the requested deferred rebasing period. In its response, Hydro One proposes amendments to the proposed rate schedules filed in Attachment 9 of the application as set out below:

[7] Hydro One acquisitions – Norfolk Power Distribution Corporation (EB-2013-0196); Haldimand Hydro (EB-2014-0244); Woodstock Hydro (EB-2014-0213)

Current Rider Description	Proposed Rider Description or Amendment
Rate rider for application of tax changes (2016) – effective until April 30, 2017	Rate rider for application of tax changes – effective until the effective date of the next cost of service application
Rate Rider for Disposition of Account 1576 - effective until December 31, 2016 - Approved on an Interim Basis	Delete as Rider has expired

OEB staff makes the following submissions with respect to Hydro One's proposal:

1. <u>Rate rider for application of tax changes (2016) – effective until April 30, 2017</u>

   Hydro One proposes to amend the description of this rate rider by changing the sunset date. OEB staff notes that the treatment of tax sharing differs between the three previously acquired distributors (Norfolk, Haldimand and Woodstock). The OEB approved a debit tax sharing rider for the Norfolk service territory that is effective until the effective date of the next cost-based rate order. No tax sharing was embedded on the tariffs of Haldimand or Woodstock. Given that it's a credit rider, OEB staff has no concerns with applying the Norfolk treatment to the Orillia Power service territory. However, OEB staff notes that Orillia Power has an updated rate rider approved for the application of tax changes in its 2017 IRM application (EB-2016-0321). OEB staff assumes that this most recent set of riders will be the ones that will be embedded on Orillia Power's Tariff of Rates and Charges until the effective date of the next cost-based rate order.

2. <u>Rate Rider for Disposition of Account 1576 – effective until December 31, 2016 – Approved on an Interim Basis</u>

   Hydro One proposes to delete this rate rider as it has expired. Orillia Power was approved to dispose the balance of Account 1576 as at December 31, 2014 on an interim basis in EB-2015-0286. In that application, Orillia Power proposed to continue to use Account 1576 until such time as a final disposition is approved during its next cost of service application. The rate rider pertaining to the approved Account 1576 balance expired on December 31, 2016 and does not appear on Orillia Power's most recent (2017) Tariff of Rates and Charges. Therefore, OEB staff submits that the rate rider has been already been removed and the Panel in this application does not need to make a finding in this regard.

However, OEB staff submits that Account 1576 pertaining to the Orillia Power service territory should continue to be used until its next cost-based rate application following the conclusion of the deferred rate rebasing period. OEB staff addresses this matter further below in the Accounting Standard section.

3.3 Other Requested Approvals

As part of the application, the applicants make the following additional requests.

Tracking of Deferral and Variance Accounts

Hydro One requests OEB approval to continue to track costs to the deferral and variance accounts (DVAs) currently approved by the OEB for Orillia Power and to seek disposition of their balances at a future date. In its interrogatory responses[8], Hydro One indicates that it will comply with the *Report of the Board on Electricity Distributors' Deferral and Variance Account Review Report* and request disposition of Group 1 accounts accordingly. Hydro One also confirmed that it will track Orillia Power's DVAs separate from its own accounts.

[8] Exhibit 1, Tab 1, Schedule 10, OEB Staff IR#10

OEB staff submits that approval to track costs to the DVAs should be granted. Similar requests were filed as part of other previous consolidation applications and were granted by the OEB[9]. OEB staff also submits that disposition of Group 2 accounts should be consistent with OEB's policy. However, OEB staff recognizes that 10 years is a long time for Group 2 accounts not to be disposed. These accounts can be either credits or debits to customers. Therefore, OEB staff submits that Group 2 accounts should be cleared at least every five years, as would be the case for a non-consolidating distributor on the Price Cap IR rate-setting option. This could be done in a stand-alone application.

New Regulatory Account for ESM cost tracking

The application states that a regulatory account is required to track costs associated with the ESM. In response to OEB Staff Interrogatory No. 15, Hydro One confirms that it is seeking the OEB's approval through this application for the establishment of a regulatory account to track costs associated with the ESM. If approval is granted, Hydro One intends to submit a draft accounting order for the OEB's approval either as a condition of the approval of the application or as a subsequent filing.

OEB staff supports Hydro One's request for the establishment of a deferral account to track costs associated with the ESM but makes no submissions on the amount proposed to be recorded in the account or the disposition of this account as these are rate matters which lie outside the scope of this proceeding. OEB staff submits that a separate application will need to be made for the disposition of this account and will be subject to a prudence review by the OEB at the time.

Accounting Standard

Orillia Power uses Modified International Financial Reporting Standards (MIFRS) for

[9] LDC Co. (EB-2016-0025), Hydro One and Haldimand County Hydro Inc. (EB-2014-0244), Hydro One and Woodstock Hydro Services Inc. (EB-2014-0213)

regulatory accounting purposes and Hydro One uses United States Generally Accepted Accounting Principles (USGAAP) for regulatory accounting purposes. Hydro One is requesting approval to use USGAAP for regulatory accounting purposes in relation to Orillia Power. Hydro One submits that it would be inefficient and costly to maintain two different accounting regimes for divisions within Hydro One, arguing that by using one uniform standard of reporting, Hydro One seeks to achieve integration and scale efficiencies.

Should the OEB decide to grant this application, OEB staff submits that the request to use USGAAP should also be granted. Similar requests were filed in other Hydro One acquisition proceedings[10] and were granted by the OEB.

In its interrogatory responses[11], Hydro One indicates that it anticipates property, plant and equipment (PP&E) and post-retirement benefits and related deferred taxes to be impacted upon transition from IFRS to USGAAP. Hydro One states that it will stop recording entries into Account 1575 IFRS-CGAAP Transitional PP&E Amounts and Account 1576 Accounting Changes Under CGAAP, which captured MIFRS transitional impacts to PP&E if the OEB approves the acquisition transaction[12].

Hydro One also indicates[13] it does not plan on requesting a deferral account for any material accounting standard transition adjustments that impact revenue requirement. Hydro One does not explain why.

OEB staff notes that in the *Addendum to the Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment*, the OEB only approved the establishment of a generic PP&E deferral account relating to the transition to MIFRS. The OEB did not approve any other deferral account on a generic

[10] Hydro One and Norfolk Power Distribution Inc. (EB-2013-0187), Hydro One and Haldimand County Hydro Inc. (EB-2014-0244), Hydro One and Woodstock Hydro Services Inc. (EB-2014-0213)
[11] Exhibit 1, Tab 5, Schedule 8, SEC IR #8
[12] Exhibit 1, Tab 3, Schedule 5, VECC IR #5, Exhibit 1, Tab 5, Schedule 17 SEC IR #17
[13] Exhibit 1, Tab 1 Schedule 16, OEB Staff IR #16

basis but noted that utilities could request individual accounts if they can demonstrate the likelihood of a large impact upon transition to MIFRS. The report also indicated that utilities that report under USGAAP should read references to MIFRS in the report to include USGAAP.

OEB staff submits that in the case where the transition to USGAAP results in a material revenue requirement impact that could potentially be refunded to ratepayers, a deferral account would be required to capture the potential refund. Without a deferral account to capture any potential transition impact that is favourable to ratepayers, there would be no opportunity to do so after that, as any adjustments to prior period rates would constitute retroactive ratemaking.

OEB staff submits that the OEB should establish a deferral account relating to a material transition impact that is favourable to customers. The OEB should be the one to determine whether a potential refund to ratepayers from the transition to another accounting standard should be returned to ratepayers upon the requested disposition of such an account. Hydro One should not be the one to decide this simply by forgoing such an account. OEB staff notes that the establishment of a deferral account does not guarantee the disposition of the account as the account will be subject to a prudence review in a subsequent rate application.

Hydro One has proposed to discontinue Account 1575 and Account 1576 if the acquisition is approved. OEB staff notes that these two accounts are to capture the differences in changes in accounting policies and accounting standards made during an IRM period until a distributor's next cost-based rate application. Included in these impacts are the impacts arising from a change to useful lives. OEB staff submits that the intent and nature of these accounts should continue until the next cost-based rate application for the Orillia Power service territory following the end of the the deferred rate rebasing period, and not just until it is acquired by Hydro One (if approved), as proposed by Hydro One. As such, if the OEB accepts Hydro One's proposal to discontinue Accounts 1575 and 1576, the new account that OEB staff has referenced above should continue to capture these items as well as any new transition impacts from the adoption of USGAAP.

Amendment and Cancellation of Licences

Orillia Power requests that after the transfer of the distribution system to HONI is completed, its electricity distribution licence be cancelled and that HONI's licence be amended at the same time, authorizing HONI to serve Orillia Power's customers.

OEB staff supports the proposed licence changes.

4 CONCLUSION

OEB staff submits that the evidence provided by the applicants reasonably demonstrates that the proposed acquisition of Orillia Power by Hydro One meets the no harm test. Accordingly, OEB staff submits that the transactions proposed to effect the acquisition of Orillia Power by Hydro One should be approved.

All of which is respectfully submitted.