Ontario Energy Board
Commission de l'énergie de l'Ontario

DECISION AND ORDER

EB-2016-0160

HYDRO ONE NETWORKS INC.

2017 and 2018 Transmission Revenue Requirements and Charge Determinants

BEFORE: **Ken Quesnelle**
Presiding Member

Emad Elsayed
Member

Peter C. P. Thompson, Q.C.
Member

November 9, 2017

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1. INTRODUCTION AND SUMMARY

This Decision and Order determines issues related to the draft revenue requirement/charge determinant order and draft uniform transmission rates (UTR) order and supporting materials (collectively the DRO) filed with the Ontario Energy Board (OEB) by Hydro One Networks Inc. (Hydro One) on October 10, 2017. These DRO materials were filed pursuant to the OEB's September 28, 2017 EB-2016-0160 Decision and Order pertaining to Hydro One's 2017 and 2018 transmission revenue requirements and charge determinants (Decision).

The OEB received submissions pertaining to the consistency of the DRO with the Decision from OEB staff, several intervenors and Hydro One. The issues raised by these submissions included matters pertaining to the following topics:

(i) The appropriate figure to use for the 2017 revenue requirement of Canadian Niagara Power Inc. (CNPI)

(ii) The changes in forecast capital spending and in-service additions over the 2017 - 2018 period and whether there was a sufficient explanation for them

(iii) The regulatory income tax amounts that should be reflected in the DRO

(iv) The calculation of the foregone transmission revenue amount.

The OEB's findings regarding these matters are provided in sections that follow entitled:

- CNPI Revenue Requirement and Deferral Account Request
- 2017 - 2018 Capital Spending and In-Service Additions forecasts
- Regulatory income taxes recoverable from ratepayers
- Foregone transmission revenue deferral account.

Matters not in dispute are approved in this Decision and Order in sections entitled;

- 2017 and 2018 Charge Determinants
- 2017 Other Charges
- Accounting Orders.

2. THE PROCESS

The Decision, released on September 28, 2017, required Hydro One to file:

(a) Drafts of a revenue requirement/charge determinant order and a UTR order along with supporting schedules

(b) A revision to Exhibit J11.3 separating the amounts in the “FMV in excess of Tax Basis” column between their “recapture” and “gain” components, along with a reconciliation of the “recapture” amounts to certain information contained in financial statements filed in evidence in the proceeding

(c) Calculations of the grossed up regulatory taxes recoverable from transmission ratepayers in 2017 and 2018 derived by multiplying taxes, calculated for each of those years under an assumed 100% allocation to shareholders of future tax savings benefits, by the 71% recapture ratio for transmission.

Hydro One complied with the Decision’s filing requirements on October 10, 2017. The documents filed included a covering letter, a five-page document entitled “Implementation of the Decision, October 10, 2017” and “Supporting Materials” labelled DRO Exhibits 1 to 10 inclusive.

Hydro One is one of five licensed electricity transmitters in Ontario that recover their revenues through Ontario's UTR. The OEB approves the revenue requirements and charge determinants for the individual transmitters and uses them to calculate the UTR. The Decision determined that the 2017 UTR will be effective January 1, 2017 but implemented October 1, 2017.

The total amount to be recovered by Hydro One Transmission in 2017 is derived from the OEB's EB-2016-0160 Decision. The findings in this Decision and Order will lead to the finalization of the transmission revenue requirement amounts, charge determinants and related matters for Hydro One in 2017 and 2018. For 2017, these amounts will be approved on a final basis. The 2018 revenue requirement will be adjusted in a 2018 cost of capital update when the OEB’s cost of capital parameters are issued, and will be finalized in a separate process leading to the issuance of the 2018 UTR.

The final 2017 amounts to be approved as a result of this Decision and Order will be used in the determination of the 2017 UTR along with the related amounts approved for the other four Ontario transmitters. The 2017 UTR rate order will be completed under OEB file number EB-2017-0280.

Hydro One’s draft order seeks approval for a total 2017 rates revenue requirement of $1,445.3 million, along with the charge determinants and the percentages for allocating these revenues to the three transmission rate pools. Hydro One also included in its DRO materials the 2018 revenue requirement, but this amount will be adjusted in the near future when the OEB issues its 2018 Cost of Capital parameters. These costs will be included in the 2018 UTR to be issued in late December 2017 or early January 2018.

OEB staff and six intervenors filed their comments on the DRO materials on October 16, 2017. In addition, one other Ontario transmitter, CNPI, filed comments on the draft Revenue Requirement and Charge Determinant Order. Hydro One replied to those comments on October 18, 2017. Accompanying this reply submission were supporting materials labelled as DRO Reply Submission Attachments 1 to 5 inclusive.

3. CNPI REVENUE REQUIREMENT AND DEFERRAL ACCOUNT REQUEST

In the DRO materials, Hydro One used a 2017 transmission revenue requirement for CNPI of $4,457,953. In its October 13, 2017 submissions, CNPI indicated that its 2017 transmission revenue requirement for use in the UTR calculation should be $4,647,201, as the previous total included the disposition of deferral accounts in 2016 which are not applicable outside of the 2016 rate year. Hydro One made changes to the DRO materials to reflect this amount.

In its submission, CNPI also asked the OEB to create for it a 2017 Lost Revenue Deferral Account in the UTR proceeding EB-2017-0280 identical to the one that the Decision establishes for Hydro One.

Findings

The OEB accepts a 2017 revenue requirement amount for CNPI of $4,647,201 for use in the UTR calculation. However, the OEB finds that the requested 2017 Lost Revenue Deferral Accounting Order should not be addressed in this Hydro One proceeding. CNPI's application for that accounting order should be made in a separate OEB process.

4. 2017-2018 CAPITAL SPENDING AND IN-SERVICE ADDITIONS FORECASTS

a) 2017-2018 Capital Forecast

In the DRO materials, Hydro One provided reduced capital spending forecasts in each of the sustaining, development, operations and common corporate cost categories of expenditure to achieve the $126.1 million reduction in 2017 and the $122.2 million reduction in 2018 directed in the Decision.

In their DRO submissions, OEB staff and several intervenors questioned the lack of detailed project information related to the reductions in forecast expenditures and whether these reductions were consistent with the OEB Decision. These parties criticized Hydro One for the concentrated capital spending reductions in the development category when the Decision focused on the magnitude and pacing of the sustaining capital program. They suggested that the OEB require Hydro One to elaborate on its rationale for allocating reductions among the four categories of expenditure and how this allocation is consistent with the Decision.

With its DRO reply submission, Hydro One provided a new table of adjusted forecast capital spending that corrected clerical errors in the initially filed materials. This material reflects the forecast changes in in sustaining, development, operating and common corporate cost capital spending at the sub-category level.

Hydro One explained that its capital reductions were based on the current status of its capital projects and programs, execution risks and overall capital planning and redirection processes as of the September 28, 2017 date of the Decision, being just before the fourth quarter of 2017 and almost half way through the 2017 and 2018 rate term.

Hydro One advised that reductions in sustaining capital forecasts reflected slowed pacing of tower coatings and stations and line investments. Development capital forecast reductions reflected changes in customer demand and project forecasts. Hydro One advised that there may be further changes in demand-driven capital expenditures before the 2017-2018 rate term ends and that it will manage within the OEB-approved capital envelope accordingly.

Findings

The OEB finds that the information provided by Hydro One, both in the DRO and the DRO reply submission, is insufficient to enable the OEB to determine whether the proposed changes in capital spending forecast are consistent with the Decision.

The Decision regarding reductions in proposed capital spending for 2017 and 2018 focused entirely on the lack of full justification for the sustaining capital category; mostly the transmission stations sub-category and the tower coating program in the transmission lines sub-category.

While the OEB-imposed reduction in total capital spending for both years combined represented 11.3% of the proposed spending, the DRO reply submission (Table 1) shows that the proposed reduction in sustaining capital is only 4.9%. Furthermore, the breakdown of that reduction by sub-category (Attachment 2 of the DRO reply submission) shows that the forecast for transmission station capital has actually been increased by approximately 4.3% for both years combined. The tower coating program is not specifically listed in the breakdown of the transmission lines component in Attachment 2 of the DRO reply submission.

On the other hand, the proposed reduction in the development category, which was not a subject of specific OEB concerns in its Decision, is much higher (38.2% for both years combined). According to Hydro One, these reductions were mostly driven by timing and customer demand.

The OEB finds that the explanations provided by Hydro One in its DRO reply submission did not provide a complete rationalization of the proposed allocation of the reductions among the capital spending categories. The OEB recognizes that, given the date of its Decision, there is limited flexibility for Hydro One to adjust 2017 projects that are already underway or are at an advanced stage of planning. The OEB believes that there is more flexibility for projects which are planned to start in 2018 or for ongoing programs such as tower coating.

The OEB directs Hydro One to seek further opportunities to address the concerns raised in the OEB Decision regarding sustaining capital and to report on the specific actions taken and their impact as part of the status report which was required by the OEB in section 4.4 of its Decision. This part of the report should describe how the actions taken and associated results are consistent with the wording and intent of the Decision. This information would enable future OEB panels to determine whether any of the proposed additions to rate base should be denied.

The OEB emphasizes that Hydro One is exposed to the risk of disallowance of proposed rate base additions in future test periods for actual capital expenditure amounts that are materially and unjustifiably incompatible with the capital expenditure concerns expressed in the Decision.

b) 2017-2018 In-Service Additions (ISA) Forecast

In the DRO materials, Hydro One calculated that the $126.1 million capital budget reduction in 2017 would result in a reduction of $63.7 million of ISA in that year. The 2018 budget reduction of $122.2 million was forecast to produce $31.3 million of ISA reduction in that year.

Several parties questioned the disparity between the annual budget reductions and the materially lower annual ISA reductions. Certain intervenors asked the OEB to impose higher ISA reductions for 2017 and 2018 by applying an overall capital expenditure to ISA ratio (CAPEX to ISA ratio) derived from the evidence filed in support of the application for 2017 and 2018. Applying this ratio would increase the ISA reductions for 2017 and 2018 from the $63.7 million and $31.3 million amounts contained in the DRO materials to $109.2 million for 2017 and $131.7 million in 2018.

Hydro One criticized this proposed approach as overly simplistic and incorrect especially in relation to capital spending for work already in execution. Hydro One suggested that it would be imprudent for it to halt projects that are planned to be placed in service in 2017. It submitted that the overall CAPEX/ISA ratio approach does not align with the reality of operating a business with multi-year construction projects and that there is no evidentiary basis to support this proposal. Hydro One also noted that, to the extent that actual ISA are lower than forecast, the asymmetrical in-service variance account protects ratepayers against the risk of over-collecting related costs.

Findings

For the same reasons described in the previous section, the OEB does not have sufficient information to judge the adequacy of the proposed ISA reductions. The status report requested by the OEB in section 4.4 of its Decision already requires Hydro One to report on actual ISA compared to plan. In addition, the OEB directs Hydro One to specifically describe in that report how the actions taken by Hydro One to meet the intent of the Decision regarding capital reductions affected ISA. This information would enable future OEB panels to determine whether any of the proposed additions to rate base should be denied.

5. REGULATORY INCOME TAXES RECOVERABLE FROM RATEPAYERS

The DRO materials included, as DRO Exhibit 2.1 Attachment 1, a revision to Exhibit J 11.3 to separate the "FMV in excess of Tax Basis" between its "recapture" and "gain" components. Hydro One's DRO reply submission Attachment 4 confirms that the recapture ratio for Hydro One Networks is 50% instead of the 77% ratio estimated in the Decision. This attachment also confirms that the recapture ratios for transmission and distribution are 52.5% (rounded to 53%) and 47.4% (rounded to 47%) instead of the 71% and 84% estimates in the Decision.

The adjusted recapture ratio for transmission of 52.5% is lower than the percentage allocation to shareholders of 62% under the allocation factor methodology established in the Decision for applying the benefits follow costs principle in the partial share sale scenario where 51% of the shares initially held by the Province of Ontario (Province) have actually been sold at fair market value (FMV).

DRO Exhibit 2.2 contains Hydro One's calculations of the grossed up regulatory taxes in 2017 and 2018 derived by multiplying taxes calculated for each of those years under an assumed 100% allocation to shareholders of the future tax savings benefit by the Decision's estimated recapture ratio of 71%.

The DRO materials do not contain a calculation of the regulatory taxes amounts derived by applying a multiple of 62% to taxes calculated under an assumed 100% allocation to shareholders of the future tax savings. No calculation of this nature was provided in the DRO materials even though the methodology established by the Decision for applying the benefits follow costs allocation principle produces a transmission allocation factor in favour of shareholders of 62%, which is higher than their recapture ratio allocation factor of 52.5%.

SEC, supported by other intervenors, provided DRO submissions on the regulatory taxes adjustment issue. SEC submitted that, as a result of the additional tax-related information provided by Hydro One pertaining to the calculation of the recapture ratios, the recapture ratio for transmission needed to be adjusted and reduced to 52.5%.

SEC submitted that the Decision required the benefit follows costs "Actual FMV Sales and Payments" allocation factor to be applied to derive regulatory taxes recoverable from transmission ratepayers when that allocation factor exceeded the recapture ratio allocation factor in favour of shareholders.

SEC submitted that the "Actual FMV Sales and Payments Ratio" applied to an allocation of the future tax savings benefits attributable to the goodwill component of the FMV Bump.

SEC proposed an increase to 63.5% of the Decision's Actual FMV Sales and Payments Ratio for transmission of 62%. SEC's rationale for this proposal was the Province's yet to be completed commitment to transfer to First Nations a 2.5% share interest in Hydro One Limited. Applying its proposed ratio of 63.5%, SEC calculated the regulatory taxes recoverable from transmission ratepayers to be \$52.2 million for 2017 and \$56.4 million for 2018.

SEC also asked the OEB to establish a deferral or tracking account to be used to verify that transmission ratepayers receive, over time, their 36.5% share of the transmission related deferred tax asset having a value of \$1,476 million.

Apart from filing DRO reply submission Attachment 4, confirming the adjusted recapture ratios, Hydro One did not make any specific submissions in response to SEC's tax adjustment submissions. Hydro one did refer to the process in which it was then engaged to prepare and file a Motion to Review and Vary the Decision, part of which concerned the correctness of the income tax section and its formulation of the allocation methodologies. That motion was filed with the OEB on October 18, 2017.

Findings

5.1 Regulatory Income Taxes

For the reasons that follow, the OEB finds that the regulatory income taxes amounts to be approved for recovery in transmission rates are \$51.0 million for 2017 and \$55.0 million for 2018.

An overview of certain facts in the record and findings in the Decision is necessary to provide the context for these regulatory tax recovery findings. These facts and findings are as follows:

a) The regulatory income taxes that Hydro One sought to recover from transmission ratepayers of \$89.1 million for 2017 and \$89.6 million for 2018 were notional sums that exceeded actual income taxes payable in those years which would be zero but for Ontario minimum tax amounts[1].

b) Hydro One's calculation of these amounts presumed an allocation to shareholders of 100% of the future tax savings benefit of almost \$2,600 million.

[1] EB-2016-0160 Decision and Order, September 28, 2017 (Decision) at pages 55-56.

c) The event giving rise to the $2,600 million tax shield was the Province's sale, in November of 2015, of more than10% of its shares in Hydro One Limited pursuant to an initial public offering (IPO) outlined in a prospectus dated October 29, 2015 (Prospectus).[2]

d) In the Prospectus, Hydro One Limited acknowledged and warned that there was a risk that the OEB might not accept the 100% allocation to utility shareholders of the future tax savings benefit. The Prospectus stated that the OEB might apportion the benefit between utility shareholders and ratepayers or allocate the entire benefit to ratepayers. An acknowledgement and warning to the same effect was included in Hydro One Limited's 2015 Annual Report.[3]

e) About 15% of the Provinces shares in Hydro One Limited were sold in early November 2015. These shares were sold at FMV. Under the provisions of the federal Income Tax Act (ITA), upon the sale by the Province of more than 10% of its shares, Hydro One Limited was 'deemed" to have sold and reacquired all of its assets at FMV. In this case, the share sale that triggered the "deeming" provisions of the ITA was a sale at FMV.

f) As of November 2015, about 15 % of the shares in Hydro One Limited had actually been sold at FMV. The remainder were held under the auspices of the "deemed" sale and reacquisition at FMV under the ITA.

g) The Decision identified the issue to be determined as one related to the allocation of a future tax savings benefit between utility shareholders and ratepayers.[4]

h) The Decision found that an issue of allocation between utility shareholders and ratepayers is a function that falls within the OEB's ratemaking authority.[5]

i) The Decision found that the "stand alone" principle did not apply to prescribe a 100% allocation of the benefit to shareholders.[6]

j) Issues pertaining to the allocation of future tax savings benefits that arose as a result of a "deemed" acquisition of utility assets at FMV had been considered by the OEB in a prior proceeding that concluded with the issuance of an OEB

[2] Decision at page 83.
[3] Decision at page 106 and footnote 165.
[4] Decision at page 86.
[5] Decision at page 87.
[6] Decision at page 87.

Report in May, 2005[7] and an accompanying rate handbook. The allocation of tax benefits issue had then arisen because, in conjunction with the introduction of the provincial Payment in Lieu of Taxes (PILS) regime, all tax-exempt distribution utilities were deemed to acquire their assets at FMV as of October 1, 2001. As in this case, that deemed acquisition of assets at FMV gave rise to an FMV Bump in the value of fixed assets and goodwill and consequential future tax savings that the utilities were asking the OEB to allocate entirely to utility shareholders.[8]

k) The OEB's May 2005 Report in the RP-2004-0188 (RP-2004-0188 Report) proceeding and its accompanying handbook allocated 100% of the tax benefits associated with the FMV Bump arising from a deemed transaction to ratepayers.

l) The RP-2004-0188 Report considered issues related to the benefits follow costs allocation factor and the recapture consequences of a subsequent sale of utility assets at FMV.

m) In its argument in this proceeding, Hydro One relied upon recapture and the benefits follow costs allocation principle to support its proposal that 100% of the future tax savings benefit be allocated to utility shareholders.[9] Hydro One argued that the provisions of the RP-2004-0188 Report did not apply to support any allocation of the tax savings in this case to ratepayers.

n) The Decision rejected these arguments. The Decision found that, in circumstances where only a portion of the Province's shares had been actually sold at FMV and the remainder were held under the auspices of a legislatively "deemed" sale and re-acquisition, the RP-2004-0188 Report informed the allocation between shareholders and ratepayers of future tax savings attributable to recapture as well as the allocation of those savings between them under the benefits follow costs allocation principle.[10]

o) Having been informed by the principles expressed in the RP-2004-0188 Report the Decision found that:[11]

    (i) The future tax savings related to the portion of the FMV Bump that is attributable to recapture are to be allocated to shareholders.

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[7] Decision at page 88.
[8] RP-2004-0188 "2006 Electricity Rate Handbook", Report of the Board, (11 May 2005, at pages 55-57, and 2006 Electricity Rate Handbook, May 11 2005 (Rate Handbook).
[9] Decision at page 90.
[10] Decision at page 89.
[11] Decision at pages 89-90

(ii) The benefits follow costs principles apply to future tax savings related to the portion of the FMV Bump that has actually been sold at FMV; but not to the portion of the FMV Bump that is held under the auspices of the "deemed" sale and reacquisition pursuant to the provisions of the ITA.

(iii) The recapture allocation factor applies if it provides an allocation to shareholders that exceeds the allocation to them under the benefits follow costs allocation factor.

(iv) Conversely, the benefits follow costs allocation factor applies if it provides an allocation to shareholders that exceeds their recapture allocation factor.

p) The Decision then established separate methodologies for determining the recapture and benefits follow costs allocation factors in favour of shareholders. The Decision states that these methodologies were determined in a manner that maintained consistency with the principles expressed in the RP-2004-0188 Report and the OEB's findings in this case based thereon to achieve a reasonable balance between the interests of utility shareholders and ratepayers.[12]

q) Since the additional tax related information that the Decision required Hydro One to provide reveals that the transmission recapture ratio in favour of shareholders[13] is less than their benefits follow costs allocation factor, the recapture ratio allocation factor for transmission is now of no significance to the final determination of the regulatory taxes recoverable from transmission ratepayers in this proceeding.

r) In establishing a methodology for determining the benefits follow costs allocation factor in favour of shareholders, the Decision first found that it would be unreasonable to allocate 100% of the tax savings benefits to shareholders when, currently, less than 100% of the Province's shares have actually been sold at FMV. [14]

s) The Decision considered the manner in which the departure tax liability to the Province was discharged by a payment sourced from share subscription amounts provided by the Province in a series of non–arms' length transactions. These transactions did not assign the deferred tax asset to shareholders. These

[12] Decision at page 90.
[13] Decision at pages 90-95
[14] Decision at pages 95-103.

transactions did not operate to deprive ratepayers of the share of the deferred tax asset that remained attributable to the “deemed” sale and reacquisition at FMV, The Decision also considered other attributes of that liability that made it variable at the Province’s discretion. The Decision rejected Hydro One’s position that, in and of itself, the payment of the departure tax amount of $2,271 million supported an allocation to shareholders of 100% of the tax savings related to the FMV Bump of $9,794 million.[15]

t) However, the Decision accepted that the elimination of the departure tax liability added value to the FMV Bump compared to the amount of that bump that would have been realized had the liability not been eliminated or discharged in some fashion.[16] The Actual FMV Sales and Payments methodology that the Decision establishes for determining the benefits follow costs allocation factor in favour of shareholders treats the departure tax amount of $2,271 million as an actual payment towards the FMV Bump. This feature of the methodology benefits shareholders in the 51% Share Sold scenario by increasing the allocation ratio in their favour from 51% to 62%.[17]

u) The Decision finds that, currently, the Province has sold about 51% of its shares at FMV, and that the allocation to shareholders of future tax savings related to the FMV Bump of $9,794 million is about 62%.

v) Multiplying the “Grossed up regulatory taxes” shown in DRO Exhibit 2.2 of $82.2 million for 2017 and $88.8 million for 2018 by the benefits follow costs allocation factor in favour of shareholders of 62% produces grossed up regulatory taxes recoverable from transmission ratepayers of $51 million for 2017 and $55 million for 2018.

The foregoing facts and findings provide the context for the OEB’s consideration of the tax adjustment submissions made by SEC.

5.2 Adjustment of the Recapture Ratio

The OEB agrees with SEC and finds that the additional tax related information that the Decision required Hydro One to provide reveals that the OEB’s estimate of the recapture ratio at 71% is too high and needs to be reduced to 52.5% as shown in DRO Exhibit 2.1 Attachment 1 and confirmed by DRO reply submission Attachment 4.

[15] Decision at pages 97-101.
[16] Decision at page 101.
[17] Decision at pages 101-104 and Table 15-3.

Since the recapture ratio for transmission is lower than the benefits follows costs allocation factor in favour of shareholders of 62%, the information in Decision Tables 15-1 and 15-2, adjusted for the information contained in the DRO materials is of academic interest only. That said, in order to complete the record by reflecting the DRO information in these tables, Schedule A, as attached to this Decision and Order, contains final Tables 15-1 and 15-2 that incorporate the DRO information.

5.3 Allocation Factor to be Applied to Determine 2017 and 2018 Regulatory Taxes

The OEB agrees with SEC and finds that the Decision requires the benefits follow costs "Actual FMV Sales and Payments Ratio" allocation factor to determine the amounts of regulatory taxes recoverable from transmission ratepayers in 2017 and 2018. This allocation factor is more favourable to shareholders than their recapture allocation factor.

5.4 Actual FMV Sales and Payments Allocation Factor Applies to all FMV Bump Elements

The Decision applies this allocation factor to the entire amount of the transmission FMV Bump. As shown in Exhibit J11.3 and in DRO Exhibit 2.1 Attachment 1, the components of the FMV Bump consist of Fixed Assets, Goodwill, and Construction in Progress.

The OEB agrees with SEC's submission that the "Actual FMV Sales and Payments Ratio" allocation factor applies to the goodwill component of the FMV Bump. The OEB confirms that the Decision applies this methodology, that apportions future tax savings between shareholders and ratepayers on the basis of actual FMV sales and payments, to all elements of the FMV Bump, including goodwill. Hydro One made no DRO reply submissions on this point. Hydro One's acknowledgement and warning in the Prospectus and the 2015 Annual Report that the OEB could either apportion or allocate the entire tax benefit to ratepayers supports a finding that tax savings related to all elements of the FMV Bump were potentially allocable to ratepayers.

This finding on this issue is also supported by the fact that the tax shield relating to goodwill, like the tax shield relating to fixed assets has both "recapture' and 'gain' components. DRO Exhibit 2.1 Attachment 1 shows the recapture component of goodwill for Hydro One Networks Inc. to be $151 million. The remaining goodwill amount of $3,633 million is "gain".

This finding is also supported by the provisions of the RP-2004-0188 Report and the provisions of the Rate Handbook that accompanied the release of that report. The RP-2004-0188 Report[18] at pages 54 and 55, makes it clear that a "deemed" transaction at

[18] See footnote 8.

FMV gives rise to Eligible Capital Expenditure (ECE) value adjustments that produce future tax savings and that, in an entirely “deemed” transaction scenario, these tax savings in the ECE component of the FMV Bump are to be allocated to ratepayers along with other FMV Bump components. Goodwill is a major element of ECE.

The provisions of the Rate Handbook that accompanied the release of the RP-2004-0188 Report confirm the allocation to ratepayers of ECE value adjustments attributable to a “deemed” transaction. Section 7.2.5 of that Rate Handbook entitled “Regulatory tax treatment of Eligible Capital Expenditures (ECE)” has two subsections that deal with ECE related tax benefits.

Subsection i) deals with the “adjustment” in fair market value of ECE items that stems from the October 1, 2001 ”deemed” transaction that the OEB considered in the RP-2004-0188 Report. This subsection requires the value of such adjustments, to be allocated to the utility’s ratepayers for the purposes of determining regulatory taxes recoverable from them. The phrase “value adjustments” applies to the FMV Bump that occurs as a result of a “deemed” transaction and tax benefits stemming from these adjustments are to be allocated to ratepayers.

In contrast, sub-section ii) deals with the situation where the amount of ECE includes “purchased” goodwill. When the goodwill is actually purchased, then tax benefits associated with that purchased goodwill are to be allocated to shareholders.

The Decision’s Actual FMV Sales and Payments allocation factor achieves the same outcome. The tax savings related to the components of the FMV Bump that remain attributable to the portion of the Province’s shares that are held as a result of the “deemed” sale and acquisition under the ITA are allocable to ratepayers. When some or all of that portion of the shares are sold at FMV, then the tax savings related to the additional shares sold shift to the shareholders.

The portion of a corporate tax benefit for a pure utility that relates to a value adjustment to goodwill that has not yet actually been purchased is, for regulatory purposes, allocated to ratepayers. According to the RP-2004-0188 Report at page 56, the situation can be considered as analogous to a change in the tax rules. The tax benefit is allocated to shareholders when the goodwill is actually purchased.

The OEB finds that the Decision’s Actual FMV Sales and Payments Ratio allocation factor applies to goodwill and the other components of the FMV Bump which is an outcome that is compatible with OEB policy expressed in the RP-2004-0188 Report and its accompanying Rate Handbook.

5.5 SEC's Proposed Adjustment to the Actual FMV Sales and Payment Ratio

The OEB rejects, at this time, SEC's proposal to increase the Decision's benefits follow costs allocation ratio in favour of shareholders to 63.5% to reflect the Province's commitment to sell to First Nations a 2.5% interest in Hydro One Limited. The OEB's allocation methodology is intended to have the allocation to shareholders of future tax savings track actual share sales by the Province.

Since the sale to First Nations has not yet taken place, it would be premature to increase the Decision determined allocation factor of 62%.

The OEB would be prepared to consider pass through treatment to increases in regulatory taxes recoverable from ratepayers as a result of further sales by the Province of the shares it holds under the auspices of the deemed sale and reacquisition transaction provided for in the ITA. Hydro One is at liberty to apply for such pass through relief should further share sales by the Province take place.

5.6 Deferral or Tracking Account

At this time, the OEB sees no need for the tracking account that SEC has proposed. The OEB expects Hydro One to keep records of the amounts that it recovers from ratepayers on account of the shareholders' portion of the deferred tax asset and the amounts that ratepayers receive on account of their share of that asset.

If necessary, the appropriateness of tracking accounts related to each of these components of the deferred tax asset can be examined in Hydro One's current distribution rates case and/or in in its next transmission revenue requirement application.

Conclusion

For all of these reasons, the OEB finds that, for 2017, the regulatory income taxes to be included in the final orders related to Hydro One's 2017 and 2018 revenue requirements are to be $51.0 million and $55.0 million respectively and not the amounts of $58.4 million for 2017 and $63.0 million for 2018 presented in the DRO materials.

6. 2017 FORGONE REVENUE

In its DRO reply submission, Hydro One advised that, to be consistent with the approach followed in prior proceedings, it used forecast rather than actual 2017 charge determinants to determine 2017 foregone revenue. Hydro One also stated that the impact of using actual charge determinants would be small and well within the variance in revenues introduced as a result of rounding the UTR. Hydro One also provided an updated calculation of lost revenue.

Findings

The OEB accepts the use of forecast rather than actual 2017 charge determinants to derive 2017 foregone revenue. The calculation of the credit to ratepayers will need to be updated to reflect the OEB's finalization in this Decision and Order of the amount of regulatory income taxes to be recovered in Hydro One's 2017 revenue requirement.

7. 2017 AND 2018 CHARGE DETERMINANTS

The 2017 and 2018 transmission charge determinants for Hydro One were not at issue in the DRO process.

Findings

Hydro One's approved charge determinants to be incorporated into the calculation of the UTR for 2017 and 2018 are shown in Table 3.

Table 3
Charge Determinants (MW)

	Network	Line Connection	Transformation Connection
2017	244,866	236,891	202,461
2018	244,924	236,948	202,510

8. 2017 OTHER CHARGES

Hydro One also submitted the detailed calculations of two additional charges unique to its transmission operations: The Wholesale Meter Service and Exit Fee Schedule and the Low Voltage Switchgear Credit.

There were no comments from parties on the Other Charges as submitted by Hydro One.

Findings

The OEB approves Hydro One's 2017 Wholesale Meter Service and Exit Fee Schedule and the 2017 Low Voltage Switchgear Credit as submitted. These schedules are attached in Appendix A.

9. ACCOUNTING ORDERS

In its draft revenue requirement and charge determinant order, Hydro One included two draft accounting orders:

1) 2017 and 2018 In-Service Capital Additions Variance Account

Hydro One provided a draft accounting order to record the impact on 2017 and 2018 Transmission Revenue Requirement due to an actual amount for 2016 in-service additions that is less than $911.7 million; along with the difference between the 2017 and 2018 in-service additions embedded in 2017 and 2018 rate base and actual in-service additions in each of those years.

There were no comments from parties on the draft accounting order for the In-Service Capital Additions Variance Account.

2) 2017 Foregone Transmission Revenue Deferral Account

Hydro One provided a draft accounting order to record the difference between revenue earned by Hydro One Networks Transmission under the interim 2017 rates set at the 2016 UTR level and the revenues that would have been received under the approved 2017 UTR.

The OEB addressed some concerns raised with the calculation of foregone revenue at Section 6 of this Decision and Order. However, there were no comments from parties on the draft accounting order itself.

Findings

The OEB approves the Accounting Order for the 2017 and 2018 In-Service Capital Additions Variance Account and the Accounting Order for the 2017 Foregone Transmission Revenue Deferral Account. Both approved Accounting Orders are attached in Appendix A.

10. ORDER

Hydro One is required to promptly revise the draft revenue requirement/charge determinant and UTR order to reflect the further reductions in regulatory income taxes recoverable in 2017 and 2018. These updated materials should include an updated Implementation of Decision section, an updated supporting material section that should include any elaboration of items in the supporting material that was provided by Hydro One with its reply submissions.

As a result of this additional step in the finalization of Hydro One's transmission revenue requirement, the OEB will amend its finding in the September 28, 2017 Decision and Order and change the implementation date of the 2017 UTR to November 1, 2017, not October 1, 2017.

When the above filings have been received, the OEB will issue a final Hydro One transmission revenue requirement and charge determinant order and a 2017 UTR order with rates effective January 1, 2017 and implemented on November 1, 2017.

THE BOARD ORDERS THAT:

1. Hydro One shall file an updated draft revenue requirement/charge determinant order and the draft UTR rate order and supporting schedules (including a revised amount for foregone revenue), reflecting this Decision and Order, no later than November 16, 2017.

Cost Awards

2. Cost eligible intervenors in this proceeding shall submit their cost claims no later than 7 days from the date of issuance of this Decision and Order.

3. Hydro One Networks Inc. shall file with the OEB and forward to all parties any objections to the claimed costs within 14 days from the date of issuance of this Decision and Order.

4. Cost eligible intervenors shall file with the OEB and forward to Hydro One Networks Inc. any responses to any objections for cost claims within 21 days from the date of issuance of this Decision and Order.

5. Hydro One Networks Inc. shall pay the OEB's costs incidental to this proceeding upon receipt of the OEB's invoice.

DATED at Toronto November 9, 2017

ONTARIO ENERGY BOARD

Original Signed By

Kirsten Walli
Board Secretary

Schedule A

Hydro One Networks Inc.

Transmission

EB-2016-0160

Decision and Order

2017 and 2018 Revenue Requirements and Charge Determinants

Tables 15-1 and 15-2

(revised)

November 9, 2017

Table 15-1 (revised)
Summary of Deferred Tax by Segment
(with Gain and Recapture Components)

	FMV	Tax Basis	FMV in Excess of Tax Basis Recapture	Gain	Total	Tax Rate	Total
Transmission							
Fixed Assets	$ 9,965	$ 6,482	$ 2,843	$ 640	$ 3,483	26.5%	$ 923
Goodwill*	$ 2,692	$ 51	$ 78	$ 1,890	$ 1,968	26.5%	$ 522
Construction in Progress	$ 116	-	-	$ 116	$ 116	26.5%	$ 31
Deferred Tax Asset	$ 12,773	$ 6,533	$ 2,921	$ 2,646	$ 5,567		$ 1,476
Distribution							
Fixed Assets	$ 7,121	$ 4,845	$ 1,904	$ 373	$ 2,277	26.5%	$ 603
Goodwill*	$ 2,455	$ 26	$ 72	$ 1,743	$ 1,815	26.5%	$ 481
Construction in Progress	$ 80	-	-	$ 80	$ 80	26.5%	$ 21
Deferred Tax Asset	$ 9,656	$ 4,871	$ 1,976	$ 2,196	$ 4,172		$ 1,105
Norfolk							
Fixed Assets	$ 55	$ -	-	$ 55	$ 55	26.5%	$ 15
Goodwill*	$ -	$ -	$ -		$ -	26.5%	$ -
Construction in Progress	$ -	-	$ -		$ -	26.5%	$ -
Deferred Tax Asset	$ 55	$ -	$ -	$ 55	$ 55		$ 15
Hydro One Networks Inc.							
Fixed Assets	$ 17,142	$ 11,327	$ 4,747	1,068	$ 5,815	26.5%	$ 1,541
Goodwill*	$ 5,147	$ 77	$ 151	$ 3,633	$ 3,783	26.5%	$ 1,003
Construction in Progress	$ 196	-		$ 196	$ 196	26.5%	$ 52
Deferred Tax Asset	$ 22,485	$ 11,404	$ 4,897	$ 4,897	$ 9,794		$ 2,596

Source: DRO Exhibit 2.1, Attachment 1

* only 75% of goodwill is included in cumulative eligible capital pool. So FMV in excess of Tax Basis is calculated as 75% of the FMV less the Tax Basis.

Table 15-2 (revised)
Recapture Ratios

	(1) FMV Bump	(2) Gain	(3) Recapture (1) - (2)	(4) Recapture Ratio (3)/(1)
Transmission	$ 5,567	$ 2,646	$ 2,921	52.5%
Distribution	$ 4,172	$ 2,196	$ 1,976	47.4%
Norfolk	$ 55	-	$ -	100%
Hydro One Networks Inc.	$ 9,794	$ 4,897	$ 4,897	50%

Source: DRO Exhibit 2.1; Table 15-2 (revised)
Hydro One DRO Reply Submission, Attachment 4

Appendix A

Hydro One Networks Inc.

Transmission

EB-2016-0160

Decision and Order

2017 and 2018 Revenue Requirements and Charge Determinants

Exhibit 1.0
2017 Wholesale Meter and Exit Fee Schedule [DRO Exhibit 6.0]

Exhibit 2.0
2017 Low Voltage Switchgear Credit Schedule [DRO Exhibit 7.0]

Exhibit 3.0
2017 Foregone Revenue Accounting Order [DRO Exhibit 10.2]

Exhibit 4.0
2017 and 2018 In-Service Capital Additions Variance Accounting Order
[DRO Exhibit 10.1]

November 9, 2017

EB-2016-0160

Decision and Order

2017 and 2018 Revenue Requirements and Charge Determinants

Exhibit 1.0

2017 Wholesale Meter and Exit Fee Schedule [DRO Exhibit 6.0]

November 9, 2017

HYDRO ONE NETWORKS INC.
WHOLESALE METER SERVICE
AND EXIT FEE SCHEDULE

HYDRO ONE NETWORKS - WHOLESALE METER SERVICE

APPLICABILITY:

This fee schedule is applicable to the *metered market participants** that are transmission customers of Hydro One Networks ("Networks") and to *metered market participants* that are customers of a Local Distribution Company ("LDC") that is connected to the transmission system owned by Networks.

* The terms and acronyms that are italicized in this schedule have the meanings ascribed thereto in Chapter 11 of the Market Rules for the Ontario Electricity Market.

a) Fee for Wholesale Meter Service

The *metered market participant* in respect of a *load facility* (including customers of an LDC) shall be required to pay an annual fee of $7,900 for each *meter point* that is under the transitional arrangement for a *metering installation* in accordance with Section 3.2 of Chapter 6 of the Market Rules for the Ontario Electricity Market.

This Wholesale Meter Service annual fee shall remain in place until all the remaining meter points exit the transitional arrangement.

b) Fee for Exit from Transitional Arrangement

The *metered market participant* in respect of a *load facility* (including customers of an LDC) or a *generation facility* may exit from the transitional arrangement for a *metering installation* upon payment of a one-time exit fee of $ 5,200 per *meter point*.

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Decision and Order

2017 and 2018 Revenue Requirements and Charge Determinants

Exhibit 2.0

2017 Low Voltage Switchgear Credit [DRO Exhibit 7.0]

November 9, 2017

Hydro One Networks Inc.
Implementation of Decision with Reasons on EB-2016-0160

Low Voltage Switchgear (LVSG) Credit
Effective January 1, 2017

Charge Determinant (MW) *(Note 1)*	**Transformation Pool Revenue Requirement Before LVSG Credit ($M)** *(Note 2)*	**Rate Before LVSG Credit ($/kw/month)**	**Total Annual 2017 NCP Demand for Toronto Hydro and Hydro Ottawa (MW)** *(Note 3)*	**LVS Proportion (%)** *(Note 4)*	**Final Annual LVSG Credit ($M)** *(Note 5)*
(A)	(B)	(C) = (B)/(A)	(D)	(E)	(F) = (C)x(D)x(E)
202,461	407.1	2.0	35,132	19.0%	13.4

Note 1: Per Exhibit 5.0

Note 2: Equals Total Revenue Requirement for Transformation Connection Pool less Non-Rate Revenues allocated to Transformation Connection Pool, as per information in Exhibit 3.0

Note 3: Per EB-2016-0160, Exhibit G1, Tab 3, Schedule 1, Table 6; Sum of Toronto Hydro and Hydro Ottawa total annual 2017 NCP Demand, 27,141 MW and 7,991 MW, respectively.

Note 4: Per EB-2016-0160, Exhibit G1, Tab 3, Schedule 1, page 7

Note 5: Per EB-2016-0160, Exhibit G1, Tab 3, Schedule 1, Table 6; Sum of Toronto Hydro and Hydro Ottawa total annual 2017 LVSG credit, $10,369,906 and $3,053,191, respectively.

EB-2016-0160

Decision and Order

2017 and 2018 Revenue Requirements and Charge Determinants

Exhibit 3.0

2017 Foregone Revenue Accounting Order [DRO Exhibit 10.2]

November 9, 2017

ACCOUNTING ENTRIES

FOREGONE TRANSMISSION REVENUE DEFERRAL ACCOUNT

This account records the differences between revenue earned by Hydro One Networks Transmission under the interim 2017 rates set at the 2016 Uniform Transmission Rates (UTR) level, and the revenues that would have been received under the approved 2017 UTR based on the Board approved 2017 load forecast ("Foregone Revenue"). The account will capture the Foregone Revenue from January 1, 2017 to the date when the approved 2017 UTR are reflected in the revenue earned by Hydro One Networks. The accounting entries to be recorded are as follows:

USofA#	**Account Description**
Dr/Cr: 1508	Other Regulatory Assets – Sub account "Foregone Transmission Revenue Deferral Account"
Cr/Dr: 4110	Transmission Services Revenue

To record the Foregone Revenue.

USofA#	**Account Description**
Dr/Cr: 1508	Other Regulatory Assets – Sub account "Foregone Transmission Revenue Deferral Account"
Cr/Dr: 6035	Other Interest Expense

To record interest improvement on the principal balance of the "Foregone Transmission Revenue Deferral Account".

EB-2016-0160

Decision and Order

2017 and 2018 Revenue Requirements and Charge Determinants

Exhibit 4.0

2017 and 2018 In-Service Capital Additions Variance Accounting Order
[DRO Exhibit 10.1]

November 9, 2017

ACCOUNTING ENTRIES
IN-SERVICE CAPITAL ADDITIONS VARIANCE ACCOUNT

To record the impact on 2017 and 2018 Transmission Revenue Requirement due to an actual amount for 2016 in-service additions that is less than $911.7 million; along with the difference between the 2017 and 2018 in-service additions embedded in 2017 and 2018 rate base and actual in-service additions in each of those years. This account will be calculated annually and interest applied consistent with the Board-approved rate. The accounting entries to be recorded are as follows:

USofA#	**Account Description**
Dr/Cr: 4110	Transmission Services Revenue
Cr/Dr: 2405	Other Regulatory Liabilities – Sub account "In-service Capital Additions Variance Account"

To record the differences between revenue requirement associated with the actual in-service capital additions during a rate year and the revenue requirement associated with the Board-approved in-service capital additions for that year.

USofA#	**Account Description**
Dr/Cr: 6035	Other Interest Expense
Cr/Dr: 2405	Other Regulatory Liabilities – Sub account "In-service Capital Additions Variance Account"

To record interest improvement on the principal balance of the "In-service Capital Additions Variance Account".