ONTARIO ENERGY BOARD EB-2017-0049

OEB Staff

CROSS-EXAMINATION COMPENDIUM

Panel 2

FINDINGS

The OEB approves the establishment of a new deferral account, effective January 1, 2018 until such time as the effective date of Hydro One's next transmission revenue requirement. In the deferral account Hydro One shall record the OPEB costs that it previously capitalized, but is no longer permitted to capitalize with the issuance of Accounting Standard Update ASU 2017-07 under US GAAP.

The amount of $11 million forecast by Hydro One for these OPEB costs is material. While the OPEB cost itself is part of the 2018 revenue requirement, the new accounting standard raises a question of whether the cost should be capitalized or expensed. With the establishment of the deferral account, the OEB does not need to make that determination now, and all regulatory options remain open. The matter of capitalization is a long-term consideration that requires careful analysis within the OEB's established rate regulated framework.

In its decision in the last proceeding for Hydro One's transmission revenue requirement (the Transmission Decision), the OEB provided findings on Hydro One's capitalization of overheads. The March 2017 change in the accounting standard for US GAAP was not considered in that proceeding because it was issued after the record was closed. The Transmission Decision stated that:

> …the OEB shares the concerns of those who question the continued appropriateness of the large capitalization amounts that USGAAP allows compared to the amounts allowed under MIFRS regulatory accounting purposes.
>
> Hydro One's use of USGAAP for regulatory purposes in connection with its 2017 and 2018 rates revenue requirements, including the capitalization of overheads, will not be varied at this time. Separate and apart from this proceeding, the OEB will consider whether it should initiate a policy review of the appropriateness of the continued use by the utilities it regulates of USGAAP for the purpose of determining the capitalization of overhead amounts.[4]

The OEB has not initiated a generic policy review on the capitalization of overhead costs under US GAAP. Whether a review will be initiated in the future is not decided, and regardless, any such review would not likely conclude prior to the filing of Hydro One's next transmission revenue requirement application. The OEB finds it appropriate to approve a deferral account so that the OEB can consider in Hydro One's next transmission revenue requirement proceeding whether Hydro One should continue to capitalize OPEBs, despite the new US GAAP accounting standard.

[4] EB-2016-0160, Decision issued September 28, 2017, p.2

The OEB's *Filing Requirements for Electricity Transmission Applications - Chapter 2 Revenue Requirement Applications* require transmitters in section 2.5.5 to provide their capitalization policy and information on overhead costs. The extent to which capitalization of overheads will be considered in Hydro One's next transmission revenue requirement proceeding will be a matter for the OEB panel in that proceeding.

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OEB Staff Interrogatory # 215

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

Q-01-01

Interrogatory:

As per the December 21, 2017 update, the estimate of the test period OPEB costs has changed as a result of an updated actuarial valuation.

a) Please provide the updated OPEB cost amount for the test period.in a table consistent with Table 1 of Exhibit C1/Tab2/Schedule 2.

b) Please provide the updated OPEB valuation.

Response:

a) 2018 Forecast OPEB Costs ($ Millions)

2018-Forecast					
OPEB		**Transmission**	**Distribution**	**Other**	**Total**
OM&A	$M	17	26	4	47
Capital	$M	32	25	-	57
	$M	**49**	**51**	**4**	**104**

b) Please refer to the attached OPEB Valuation.

Witness: CHHELAVDA Samir

OEB Staff - Interrogatory # 2

Reference:

Request for Accounting Order, p. 3.

Interrogatory:

At the above reference, the applicant indicates that the Financial Accounting Standards Board issued ASU 2017-07 in March 2017. Given that a Decision and Order for EB-2016-0160 was not issued by the OEB until September 28, 2017, Hydro One Networks (Transmission) had ample opportunity to notify the OEB of this accounting standard change during that proceeding, which would have allowed the presiding OEB panel to determine how they wanted to handle the resulting impact to the 2018 transmission revenue requirement.

Why did Hydro One Networks (Transmission) not bring this information forward during the EB-2016-0160 proceeding?

Response:

Although, the decision was issued on September 28, 2017, Hydro One had already filed its reply argument in the EB-2016-0160 proceeding on February 16, 2017, prior to the issuance of ASU 2017-07. The filing of Hydro One's reply argument marked the close of the record for the EB-2016-0160 proceeding. Though Hydro One did not have specific guidance regarding the timing of the decision, it believed that a decision from the OEB was imminent at the time the accounting guidance was issued and Hydro One did not want to introduce new elements to the proceeding at that late stage. Hydro One also notes that the OEB has indicated in prior proceedings that it is not appropriate for utilities to propose amendments or introduce new evidence at the time of reply argument.[1]

It should be noted that prior to the issuance of ASU 2017-07, the Federal Energy Regulatory Commission (FERC) as well as the Edison Electric Institute jointly with the American Gas Association provided comments to the FASB during the comment period of the draft guidance that supported the exemption of rate regulated entities from this guidance and the parties argued that all components of net benefit costs are considered to be operating in nature and should not be excluded for capitalization. Subsequent to the issuance of ASU 2017-07 and the fact that it did not include an exemption, rate regulated entities including Hydro One assessed the impact of the guidance as well as the most appropriate way to address this impact in rate applications. As

[1] EB-2015-0003, PowerStream Inc., Decision and Order, August 4, 2016, pg. 8.

noted in Hydro One's application, the FERC has issued guidance that allows regulated entities under its jurisdiction to either continue capitalizing all components of Defined Benefit costs or adopt the provisions of ASU 2017-07.

Hydro One requested the deferral account as a mechanism to allow the continued capitalization of the costs no longer permissible for capitalization in ASU 2017-07. Once the deferral account is approved these costs will continue to be capitalized in the requested deferral account.

Subsequent to the filing of the Application, Hydro One's discussion with its Auditors has improved its understanding of the requirements surrounding ASU 2017-07, including the eligibility of utilities to continue capitalizing OPEB costs. Hydro One was advised that it could continue capitalizing OPEB costs, without the requirement of a deferral account, if approved to do so by its respective regulator. FERC has provided such an approval for regulated entities under its jurisdiction. Hydro One would welcome a policy decision from the OEB that allows the continued capitalization of the effected costs, similar to the FERC guidance. Such a decision would achieve the same objective as the requested deferral account without the additional regulatory overhead, going forward.

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c) Principles of consolidation

Government business enterprises are defined as those government organizations that i) are separate legal entities with the power to contract in their own name and that can sue and be sued; ii) have the financial and operating authority to carry on a business; iii) have as their principal activity and source of revenue the selling of goods and services to individuals and non-government organizations; and iv) are able to maintain their operations and meet their obligations from revenues generated outside the government reporting entity. The activities of GBEs are recorded in the financial statements using the modified equity method, applying the basis of reporting as stipulated by Public Sector Accounting Standards for GBEs. Their combined net assets are included in the financial statements as Investment in Government Business Enterprises on the Consolidated Statement of Financial Position, and their net income is shown as a separate item, Income from Investment in Government Business Enterprises (GBEs), on the Consolidated Statement of Operations. Less than wholly owned GBEs (e.g., Hydro One Limited) are reflected using the modified equity method based on the percentage of ownership government held during the fiscal year.

The Province is accounting for the results for Hydro One Limited and Ontario Power Generation based on their results prepared using International Financial Reporting Standards (IFRS) basis (including IFRS14). See Note 16 for further details regarding change in accounting policy.

In reply, Hydro One indicated that it is cognizant of the benchmarking concerns of the intervenors and that it will respond in its next rates case. Hydro One stated that it believes that it will continue to benchmark with other local utilities and that OM&A cost comparisons can still be made with appropriate top-down adjustments.

Hydro One submitted that total cost benchmarking will be more of a challenge as time passes due to the inclusion of depreciation expenses in total costs. Hydro One stated that it will work toward developing solutions to allow appropriate total cost benchmarking in the short and longer term. However, Hydro One cautioned that, as the Board and its expert has recognized in the past, there is a difficulty in benchmarking Hydro One distribution to other Ontario LDCs due to the fundamental differences in their businesses.

Capitalization

SEC expressed concern, as it did in the Transmission USGAAP proceeding, regarding the high level of overhead capitalized by Hydro One compared to other utilities. SEC noted that the Board, in the EB-2011-0268 Transmission Decision, directed Hydro One to do a comparative analysis of its capitalization policies and report in its "next rate application". SEC requested that the Board, in its decision in this proceeding, to specify that the comparative analysis should apply to distribution as well as transmission, and the report should be filed in the rate applications for both transmission and distribution.

Also, as noted above, SEC submitted that Hydro One should integrate the study of its capitalization policy with its benchmarking efforts.

Board staff, as noted above, submitted that as part of Hydro One Distribution's next cost of service application, it should include the results of its capitalization review, including information with respect to what other Ontario distributors or comparable distributors to Hydro One in Canada or US typically capitalize. The evidence should include information regarding the capitalization policies and methodologies used, with a view to comparing these to Hydro One's capitalization policies.

In its reply submissions, Hydro One indicated that it will respond as directed in the EB-2011-0268 Decision and notes that it utilizes the same overhead capitalization methodology in both Transmission and Distribution, so that issue will be addressed at that time.

2012 Distribution Rate Application

In its submissions, CME also focused on the fact that Hydro One has chosen not to file a distribution rate application for 2012 rates, and that its currently approved 2011

2014-0140). This treatment was continued in Hydro One Distribution's last cost of service application as well (EB-2013-0416).

The Hydro One pension cost allocated to Hydro One Networks is based on the ratio of base pensionable earnings for Hydro One Networks' staff, as compared to the total base pensionable earnings for all of Hydro One employees. The method of allocation of the pension cost is consistent among all shared services costs, for operating and capital costs, and is consistent with the methodology reviewed during RP-2005-0020/EB-2005-0378, EB-2006-0501, EB-2007-0681 and EB-2008-0272, EB-2009-0096, EB-2010-0002, EB-2012-0031 and 2014-0140.

For the Distribution business, the charge to be recovered through rates in 2018 is provided in Table 1 below.

Table 1: 2018 Forecast Pension Costs ($ Millions)

2018 - Forecast Corporate Pension Costs		**Transmission**	**Distribution**	**Other**	**Total**
OM&A	$M	11	17	2	30
Capital	$M	21	20		41
	$M	**32**	**37**	**2**	**71**

2. ACTUARIAL CALCULATION

The most recent actuarial valuation for the Plan was as at December 31, 2016. In May 2017, Hydro One filed this actuarial valuation with the Financial Services Commission of Ontario ("FSCO"). The valuation showed that the Plan had a surplus of $434 million, on a going-concern basis. Starting in 2017, the required contribution for the Hydro One

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(2) Subject to subsections (2.1) and (2.1.1), an employer who is required to make contributions under a pension plan or, if a person or entity is required to make contributions under the pension plan on behalf of the employer, that person or entity and, if applicable, the members of the pension plan or their representative shall make payments to the pension fund or to an insurance company, as applicable, that are not less than the sum of,

(a) in the case of a report with a valuation date before December 31, 2017, all contributions, including contributions in respect of any going concern unfunded liability and solvency deficiency and money withheld by payroll deduction or otherwise from an employee, that are received from employees as the employees' contributions to the pension plan;

(a.1) as of the date the first report with a valuation date on or after December 31, 2017 is filed under section 3, 13 or 14, all contributions, including contributions for the provision for adverse deviations in respect of the normal cost, any going concern unfunded liability, solvency deficiency and reduced solvency deficiency, and money withheld by payroll deduction or otherwise from an employee, that are received from employees as the employees' contributions to the pension plan;

(b) all contributions required to pay the normal cost;

(b.1) as of the date the first report with a valuation date on or after December 31, 2017 is filed under section 3, 13 or 14, all contributions required to pay the amount equal to the provision for adverse deviations in respect of the normal cost determined in accordance with section 11.1;

(c) all special payments determined in accordance with section 5;

(c.1) all special payments determined in accordance with sections 5.6, 5.6.1, 5.6.2 and 5.6.3; and

(d) all special payments determined in accordance with sections 31, 32 and 35 and all payments determined in accordance with section 31.1. O. Reg. 712/92, s. 3 (2); O. Reg. 73/95, s. 2 (1); O. Reg. 116/06, s. 4 (2-4); O. Reg. 239/09, s. 2;

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Section 3: Contributions

3.1 Estimated Minimum Employer Contribution

Year		2017		2018		2019
Employer Normal Actuarial Cost	$	73,261,382	$	71,354,000	$	70,650,379
Employer Normal Actuarial Cost as a % of Payroll		*13.7%*		*13.8%*		*14.0%*
Amortization Payments						
▪ Going Concern	$	0	$	0	$	0
▪ Solvency		0		0		0
Total	$	0	$	0	$	0
Application of Prior Year Credit Balance[1]		0		0		0
Application of Surplus[2]		(73,261,382)		(71,354,000)		(70,650,379)
Estimated Minimum Employer Contribution	$	0	$	0	$	0
Estimated Member Contributions		46,811,492		47,367,141		46,988,718

Notes:

[1] As at the actuarial valuation date a $48,000,000 Prior Year Credit Balance exists, which may be applied to reduce Employer contributions in 2017, 2018 or 2019.

[2] Subject to preparation of a cost certificate at beginning of year confirming updated financial position, surplus may be applied in 2018 and 2019.

3.2 Estimated Maximum Employer Contribution (Ensuing Year)

	December 31, 2016
Employer Normal Actuarial Cost	$ 73,261,382
Greater of the Unfunded Actuarial Liability and the Unfunded Hypothetical Windup Liability	3,109,514,691
Estimated Maximum Employer Contribution	$ 3,182,776,073

3.3 Timing of Contributions

Employer normal cost and member contributions: monthly and within 30 days of the month to which they pertain.

Amortization payments: monthly before the end of the month to which they pertain (or replaced by an equivalent letter of credit), if applicable.

Adjustment to contributions made since the valuation date: within 60 days from the date that this report is filed with the Pension authorities.

1.2 Reconciliation of Financial Position

Actuarial surplus (unfunded actuarial liability) as at December 31, 2015 before reflecting prior year credit balance		$ (37,687,000)
Net special payments		24,705,000
Application of:		
▪ Actuarial surplus	$ 0	
▪ Prior year credit balance	0	0
Expected interest on:		
▪ Actuarial surplus (unfunded actuarial liability)	$ (2,035,098)	
▪ Net special payments	658,265	
▪ Application of actuarial surplus	0	
▪ Application of prior year credit balance	0	(1,376,833)
Plan experience:		
▪ Investment gains (losses)	$ 292,379,000	
▪ Salary and YMPE gains (losses)	50,654,805	
▪ Cost-of-living adjustment gains (losses)	11,039,223	
▪ Retirement gains (losses)	(3,952,266)	
▪ Withdrawal gains (losses)	(2,481,510)	
▪ Mortality gains (losses)	(10,686,136)	
▪ Miscellaneous liability gains (losses)	50,078,061	387,031,177
Change in actuarial basis:		
▪ Salary Scale assumption	$ 142,938,469	
▪ Discount Rate assumption	(81,932,506)	61,005,963
Change in plan provisions[1]		0
Actuarial surplus (unfunded actuarial liability) as at December 31, 2016 before reflecting prior year credit balance		$ 433,678,307

Note:

[1] The changes in plan provisions are prospective in nature and do not have an impact on the actuarial liabilities as of the valuation date.

OEB Staff Interrogatory # 18

Issue:

Issue 8: Is the proposed industry-specific inflation factor, and the proposed custom productivity factor, appropriate?

Reference:

A-03-01 Page: 22

Table 6 provides a summary of forecasted savings due to productivity improvements over the five-year test period 2018 to 2022. Above Table 6, Hydro One states:

> *"Specifically, the Company has taken targeted actions to implement productivity improvements as early as 2018, the rebasing year, and intends to achieve further efficiencies over the subsequent four years. While the OEB's RRF provides an incentive for utilities to achieve productivity gains during the Term, such efficiencies ultimately accrue to the benefit of ratepayers at the time of the next rebasing."*

Interrogatory:

a) Please explain whether the Corporate Common productivity savings are expensed or capitalized.

b) Expenses are "current period" costs. How do productivity savings on expensed costs "ultimately accrue to the benefit of ratepayers at the time of the next rebasing" unless the lower expenses (i.e., inclusive of productivity savings) become the starting point or trend for the forecasting expenses for the test year or test period at the next rebasing?

Response:

a) Productivity savings attributed to Corporate Common costs would first be allocated to Business Units, consistent with Black & Veatch's review of allocation of common corporate costs as described in Exhibit C1, Tab 4, Schedule 1. Once allocated to Business Units, the portion to be capitalized would follow Hydro One's overhead capitalization policy as described in Black & Veatch's review of overhead capitalization rates allocation of common corporate costs in Exhibit D1, Tab 3, Schedule 1, Attachment 1.

Witness: JODOIN Joel

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b) Expected productivity savings have been embedded into Hydro One's five year business plan, including the test year. The lower expenses and lower unit costs achieved during the plan period will become the starting point of the test period at the next rebasing.

Witness: JODOIN Joel

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OEB Staff Interrogatory # 73

Issue:

Issue 21: Does the application adequately account for productivity gains in its forecasts and adequately include expectations for gains relative to external benchmarks?

Reference:

B1-01-01 Section 1.5 Page: 7

Interrogatory:

Labour Optimization is planned to "optimize the number of high-skilled regular work staff to the level required to complete core work programs."

a) How many 'high-skilled' regular work staff does Hydro One employ?

b) How many 'high-skilled' regular work staff does Hydro One expect to employ in 2022?

c) To what extent does Hydro One expect this will impact recovery times from a potential major weather event with significant forestry effort requirements?

d) What steps is Hydro One taking to manage impacts to recovery times?

Response:

a) In response to this question, "highly skilled" employees are trades and technical employees who work in the core operations of Hydro One's distribution business. There are approximately 1,700 regular employees who would be considered highly skilled.

b) Hydro One anticipates that the number of regular skilled employees will remain constant up to the year 2022.

c) There will be no negative impacts. Hydro One remains mindful of recovery times and committed to improving current response times and reliability statistics.

d) To ensure there are no negative impacts, Hydro One is looking for operational enhancements in the following areas:
    - Crew alignment/resourcing structure (single person trouble crew, field business centre consolidation); and

- Technology/grid modernization (communicating line indicators, communicating line reclosers, remote operated switches).

Prior to operationalizing these enhancements, Hydro One is completing detailed assessments including pilots with localized implementation to ensure positive results. Once proven, Hydro One will look to implement them throughout its business and drive positive results.

OEB Staff Interrogatory # 204

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

C1-02-01 Page: 9

Interrogatory:

Table 1 shows Full Time Equivalents from 2017 to 2022 for various employee categories. For 2017 the number of Casual employees is 2802 or about 33% of the total FTEs. This ratio remains the same for 2022.

a) Does Hydro One consider the 33% ratio to be optimal in terms of casual employees?

b) Will the percentage of Casual employees be increased into the 2019 – 2022 period?

Response:

a) Hydro One does consider this ratio to be an effective use of casual resources. The use of the PWU Hiring Hall is not to replace the regular workforce but rather to enable Hydro One to supplement the regular workforce with mobile and flexible workers to perform seasonal and supplemental trades work. Hiring Hall employees are used mainly for specific skills while the regular trade employees use their multi skilled training to perform more complex work. The other category of casual employees, casual construction, perform work based on their scope clauses.

b) Please refer to Table 1 in Exhibit C1 Tab 2 Schedule 1 (page 9). There is a slight increase in the PWU Hiring Hall classification, and the casual construction resource level remains constant.

Witness: MCDONELL Keith

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OEB Staff Interrogatory # 205

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

C1-02-01 Page: 9

Interrogatory:

Has Hydro One conducted a Staffing study to compare its staffing levels to other distributors and determine the optimal staffing level for its operations?

If so, please file this study or studies, and provide a rationale for current and planned staffing numbers. If not, why not?

Response:

Hydro One has not conducted such a study. The regular and total FTE count is declining over the 2017-2022 period and, as such, it has not been a priority for Hydro One to conduct a broad and likely expensive staffing study.

Witness: MCDONELL Keith

OEB Staff Interrogatory # 206

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

C1-02-01 Page: 11-13

Interrogatory:

On these pages Hydro One summarizes efforts underway to manage the total FTE complement and increase efficiency.

Please provide the estimated savings for each initiative for the 2018 test year and future years, under the various categories: Construction (flexible workforce); Engineering (standardized processes, organizational alignment, external resources); Lines (consolidation of first line managers, outsourcing, Move to Mobile and planning for Pole Replacements); Forestry (efficiency initiatives and the "Muskoka Project"); and Stations Maintenance (temporary workforce and new scheduling tool).

Response:

The evidence referenced in C1-02-01 pages 11-13 describes the strategies and process changes Hydro One is employing to gain efficiencies in order to execute on an increasing work plan with a relatively stable FTE compliment. The strategies described in each of the work programs have not been quantified as 'savings' by Hydro One.

Any related savings opportunities that have been quantified and tracked are described in detail in Exhibit I-25-Staff-123.

Witness: MCDONELL Keith

that can be safely and efficiently planned and managed by internal staff. The current staffing strategy shows a flat regular staffing complement with a plan to utilize a combination of internal resources, engineering subcontracts, construction contracts or arrangements contracted on a fixed-price basis to execute the growth in the work program. This allows Hydro One to grow safely and acquire new capabilities quickly, while maintaining its flexibility to provide the best value to our customers.

Engineering

Hydro One is working to complete both an increasing volume of engineering work as well as advancing engineering deliverables earlier in the project lifecycle to create an intentional backlog of construction-ready projects. Despite substantially growing capital work programs, Hydro One regular staff accountable for Engineering has decreased in recent years and is anticipated to remain generally flat in the coming years.

Improved organizational alignment of different engineering functions has enabled more integrated solutions across project definition and project execution phases, and Hydro One has made a number of process and organizational improvements resulting in increased output from the engineering group. Substantial work has been done to standardize engineering processes and design packages, resulting in improved on-time delivery rates and overall project cost effectiveness. Engineering prepares the technical specifications that feed external Engineering, and acts as Owner's Engineer to ensure quality and compliance.

Resources to deliver on the growing future capital work programs is planned to be achieved through increased utilization of external engineering partners, coupled with continuous improvement of internal processes. The portion of the engineering portfolio completed externally has continued to grow over recent years, from roughly 14% in 2012 to roughly 25% in 2016, and is anticipated to reach approximately 30% through 2018.

Lines

In early 2016 Provincial Lines consolidated all Technical First Line Managers (FLMs), Supervising Technicians, Meter Technicians, Area Distribution Engineering Technicians and Meter Reader Data Collectors into one technical organization. The creation of this new more focused group ensured that resources are optimized across all the zones and that roles and responsibilities for all are clear and consistent. Provincial Lines moved all distribution project crews and apprentice crews into a single newly created zone. The purpose of this reorganization was to ensure consistent and optimum utilization of hiring hall project crews. It also allowed for more focus on apprentice development.

Outsourcing work has also provided opportunities for resource optimization by ensuring skilled internal resources are available for work programs that better align with qualifications.

Additionally, two key initiatives planned over the test period are expected to positively impact performance: Move to Mobile and the Pole Replacement Program.

The use of innovative technology, being implemented through the Move to Mobile (M2M) project, will enable real time completion and verification of data, reducing administrative office effort and increase field productivity through geographic based auto-scheduling.

The Pole Replacement program focuses on two aspects of planning. The first is to strategically select poles to be replaced based on priority and selection criteria and align this with Forestry's annual trimming cycle. The second is to bundle poles that are nearing end of life or showing premature signs of decay on the same feeder.

Forestry

While the Forestry work program increases significantly throughout the planning period, the core philosophy is to perform more work for the dollars spent. This will be accomplished by maximizing the current Forestry efficiency initiatives (e.g., the Muskoka Project) as well as looking at further opportunities to utilize mechanical crews and resource mix to continue to perform more work for the same dollars.

Stations Maintenance

The overall Stations Work Program is increasing over 2016 levels. The increases are primarily the result of the need to ramp up the PCB testing and retro-fill programs. These programs must be completed by 2025. Maintenance programs outside of the PCB program are essentially flat in Distribution. Stations is managing this by increasing its temporary workforce over the planning period while at the same time reducing its regular workforce to recognize the fact that when the PCB program is completed the overall program will be smaller in size than it is today and efficiency improvements will occur in planning, scheduling and execution.

Stations is planning to introduce a new scheduling tool in 2017 which will allow it to more effectively plan and schedule its work with greater efficiency than currently exists.

7. RECRUITMENT

Hydro One continues to hire, albeit at a lesser level than previous years, into its Apprentice and Graduate Training Programs to help address the significant wave of retirements in its critical trades, technical and engineering groups.

Since January 1, 2004, 473 graduate trainees have been hired through the Company's on-campus recruitment program. Not only do new graduates bring much needed skills but

OEB Staff Interrogatory # 207

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

C1-02-01 Page: 33

Interrogatory:

Hydro One indicates the base salary increases of 2% for MCP staff, 1% for PWU staff and 0.5% for Society staff for the IRM period. Then Hydro One states that over the test period, total compensation for the Distribution business increases by 2.5%.

Please explain how the individual increases mentioned total to the 2.5% aggregate number.

Response:

There are other compensation elements in addition to base salary that are included in total compensation. These include:

Compensation Element	**Share**
Base Pay	1.3%
Overtime	0.3%
STI	0.1%
LTIP	0.3%
Share Grants	0.1%
ESOP, Other Allowances + Lump Sums	-0.2%
Burdens	0.7%
Total Dx Compensation	**2.5%**

Witness: MCDONELL Keith

OEB Staff Interrogatory # 208

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

C1-02-01 Page: 39

Interrogatory:

In addressing the Mercer study results at point 4, Hydro One indicates, "The study does not account for the impact of Hydro One's negotiated cost-saving initiatives such as future pension benefit reductions or the updated pension valuation filed with the OEB."

a) How significant are these factors to the total results of the study?

b) When does Hydro One plan to conduct another Mercer Study?

Response:

a) The planned changes (five-year earnings averaging and 85 points for early retirement) to the Hydro One pension plans for PWU and Legacy Society employees have not been reflected in the Mercer study. The study looks at costs at a specific point in time. However, at a high-level assessment, these changes when implemented may reduce the employer-provided value of these plans to approximately 95% of the current employer-provided value, assuming the other provisions, employee contributions, and assumptions are unchanged.

b) Hydro One plans on filing a new Mercer total compensation study as part of Hydro One's upcoming transmission rate filing later this year.

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Findings

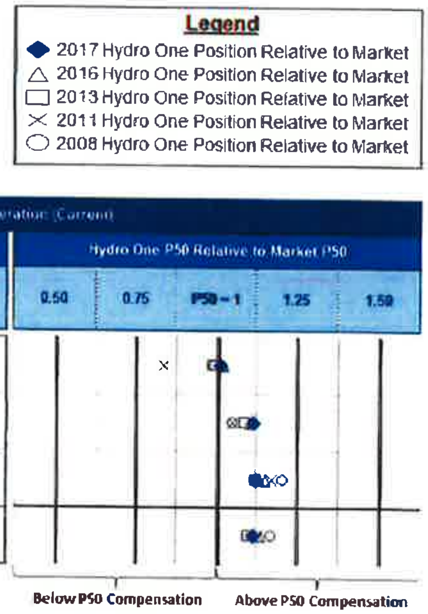
Summarized below are the results of our compensation benchmarking analysis.

Overall, **on a weighted average basis, Hydro One's total compensation cost is 12% above market median**. Hydro One is consistently positioned above the market 50th percentile for all employee groups, ranging from a low of 1% for the Non-Represented group and a high of 12% above the market P50 for the Trades and Technical group.

In the 2016 study, Hydro One's overall weighted average was 14% above the market total compensation P50 – a 2% shift towards the market median since 2016.

Table 4

			Total Remuneration (Current)				
			Multiple of P50				
	Hydro One Group	# of Hydro One Incumbents	2017 ◆	2016 △	2013 □	2011 ×	2008 ○
Weighted Average	Non Represented	172	1.01	1.02	0.99	0.83	0.99
	Energy Professionals	560	1.12	1.11	1.09	1.05	1.05
	Trades and Technical	2,478	1.12	1.16	1.12	1.18	1.21
	Overall	**3,210**	1.12	[illegible]	[illegible]	**1.13**	**1.17**



The results are driven by a combination of factors the most significant of which are the following:

- The use of casual workers that have lower cost pension and benefit packages
- Higher short-term incentive payouts to the non-represented group following strong company performance
- Highly competitive base wages, especially for the most highly skilled Power Workers' Union ("PWU") jobs (Trades and Technical Group)
- The introduction of lump sum and share grant awards to the Energy Professionals and Technical and Trades workers, respectively, in exchange for reduced base salary / wage increases, resulting in lower pension and benefit costs
- Changes in the organizations participating in the study and the benchmark job list
- The relatively high value of legacy collective agreement wages, pension and benefits programs. We note that the legacy non-represented pension and benefit and Society pension plans are now closed to new members

OEB Staff Interrogatory #S4

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

WTW Current Study, p. 3

Interrogatory:

At the above reference, background on the level structure and distribution of incumbents is provided and it is stated that:

"Full implementation of the segmented salary structures was not possible before aligning all jobs to the more structured and rigorous level framework. Using a consistent year-over-year sample, the distribution of incumbents by the new levels, compared to the legacy band structure is summarized below."

Two graphs are then shown, one labelled "Legacy Band Structure Distribution" and the other "Current Level Structure Distribution."

Please clarify how these graphs should be interpreted. For instance for the "Legacy Band Structure Distribution" at the EVP level, the numbers shown are 2 and 5. The "Current Level Structure Distribution" for the EVP level shows equivalent numbers of 11 and 5. Please provide an explanation of the differences between these two graphs that will make clear how these four numbers for all levels shown should be interpreted including what the significance is of the colour bars on each side of the graphs.

Response:

Hydro One continued its job levelling initiative in 2017, which involved a complete levelling review for all management and non- represented roles. The purpose of job levelling was to transition and align all jobs from the legacy band structure to the modernized job levels using a new job evaluation framework. A complete job levelling review was required in order to fully introduce and implement the segmented salary structures.

Witness: MCDONELL Keith

The two graphs shown on page 3 illustrate the legacy MCP Band structure and the new management and non-represented level structure. The legacy MCP bands went from MCP Band 10 (entry level) to MCP Band 1 (CEO). The new Level structure consists of 12 levels – Level 1 (entry level) to Level 12 (CEO). Legacy MCP bands 5 (Director) and 4 (VP) are now differentiated by two levels and align to variations in scopes of responsibility and provide for an additional level of granularity for each job in the levelling process. Levels 6 and 7 now align to the Director level, and Levels 8 and 9 align to the VP level.

The numbers on the right side of the legacy band structure distribution graph are intended to provide the individual incumbent distribution across each level of the MCP Bands. For instance, under the Legacy Band Structure Distribution graph, EVP – 2 and 5 refers to MCP Band 2 with five incumbents. Similarly, under Current Level Structure Distribution, EVP 11- and 5 refers to Level 11 with five incumbents. The colour bars are a visible representation of the overall distribution and number of incumbents in each level. There is no significance associated with the different shading of colour for each bar.

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OEB Staff Interrogatory #S5

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

WTW Current Study, p. 4

Interrogatory:

At the above reference, it is stated that:

"Programs must also enable attraction and retention of the talent needed to operate a regulated utility and support the growth mandate. This includes providing opportunities for career progression and supporting promotion from within, particularly within the Operations segment."

a) Please state whether or not WTW believes Hydro One's programs prior to the implementation of the programs discussed in the WTW current study, were sufficient to attract and retain talent and what the basis of this conclusion is.

b) Please discuss the indicators that demonstrate that a program of this kind is, or is not, allowing for the attraction and retention of the necessary talent and what these indicators suggest about the situation confronting Hydro One prior to and subsequent to the implementation of the WTW proposals.

Response:

a) Willis Towers Watson is not familiar with the attraction and recruitment environment prior to 2015. The programs and benchmarking approach introduced in 2015 reflect their experience working with leading organizations in managing structural costs and the ability to recruit required talent.

b) The management compensation program needs to be robust enough to attract and retain high quality talent. In particular, there have been challenges recruiting represented employees to non-represented positions mainly due to compensation related issues. Internal data analytics, similar to the compression analysis used by Willis Towers Watson on page 16 of the report, show there is a compression issue that results in compensation challenges when recruiting into some non-represented positions. Management experience from both the hiring manager and the recruitment consultant perspective based on internal and external recruitment would also suggest that it is not always possible to attract the best applicants to certain roles. Factors such as compensation and no longer having a defined benefit pension plan have been barriers to successfully attract some candidates to non-represented positions.

OEB Staff Interrogatory #S6

Issue:

Issue 40: Are the proposed 2018 human resources related costs (wages, salaries, benefits, incentive payments, labour productivity and pension costs) including employee levels, appropriate (excluding executive compensation)?

Reference:

WTW Current Study, p. 5

Interrogatory:

At the above reference, 2018 proposed compensation structure changes are discussed including proposed base salary structure changes and proposed LTIP eligibility and vehicle mix for directors.

a) Please state whether or not these changes have been implemented and incorporated into the 2018 forecast. If some or all have not, please state which ones have not been implemented and why.

b) For each of the changes listed on this page, please provide the estimated total cost increase to Hydro One on an annual basis and how this estimate was derived.

Response:

a) All of the recommendations have been implemented by Hydro One. The accepted recommendations have not changed the forecast budgets in this Application.

b)
   a. Change to base salary structure (including new structure for legal and tax positions) – no financial impact
   b. Change to LTIP Eligibility and Vehicle Mix for MCP Directors $1.2 million
   c. 2018 Merit Pay Budget of 2.5% - $2.3 M but no incremental increase to current forecast since Distribution planning assumption already included a 2.0% merit increase for MCP employees.

Total of $1.2M increase annually from 2018 onward resulting from change to LTIP Eligibility and Vehicle Mix for MCP Directors, based on current salaries and target award values calibrated to a percentage of salary.

Witness: MCDONELL Keith

- Distribution OM&A portion: $0.3 M
- Distribution Capital Expenditure portion: $0.3 M
- Distribution total impact: $0.6 M