

ONTARIO ENERGY BOARD

EB-2017-0049

Ontario Hydro Networks Inc.

Electricity Distribution Rates Application
Beginning January 1, 2018 to December 31, 2022

Submissions of the
QUINTE MANUFACTURERS ASSOCIATION

August 10, 2018

1.0 INTRODUCTION and OVERVIEW

The Quinte Manufacturers Association (“QMA” or “Association”) is pleased to have had the opportunity to participate as an active intervenor in the Custom Incentive Rate (“Custom IR”) Application (“Application”) for distribution rates that was filed by Hydro One Networks Inc. (“Hydro One”) with the Ontario Energy Board (“Board” or “OEB”) on March 31, 2017.

The QMA represents more than 120 manufacturers employing more than 9,000 people in the greater Bay of Quinte region which includes the cities of Belleville and Quinte West. Another 27,000 jobs are directly or indirectly impacted by these manufacturers. The Association assists local manufacturing leaders improve their capabilities, competitiveness and sustainability. The QMA encourages and supports a strong and healthy manufacturing sector that benefits our communities directly and contributes to continuing employment and business growth opportunities in the region.

Certainty in the delivery, reliability (security of supply), and quality of electricity is essential to the day-to-day operations of our manufacturers. They are significant users of electricity and consume more than 200 GWh of electrical energy annually. The increasing cost of electricity across the key components (generation, transmission and distribution) of the electricity market in Ontario is an active and critical concern to our members and their ability to maintain a healthy competitive advantage in the shifting global market. Our members actively manage their electricity requirements and costs. A critical component of this work is the high value QMA members place on the working relationship they have with Hydro One. That business relationship is an essential factor for our members and the communities we work in and support.

The QMA appreciates the Ontario Energy Board’s regulatory leadership in dealing with significant electricity related issues that affect all customers in these challenging economic times. The Association’s submissions below reflect specific concerns and are intended to be helpful to the Board in its deliberations on Hydro One’s Application in this proceeding. The QMA does not intend to address all the issues set out in the Board’s approved Issues

List for the proceeding. On all other issues, the QMA is in general agreement with the positions of Board Staff except where noted.

During the course of the proceeding, the QMA, undertook an extensive review and consideration of the large amount of written and oral evidence produced, and consulted regularly with its membership. The QMA participated in-person and on-line in the Technical Conference and took an active interest the oral hearing through attendance and cross-examination. In addition, the QMA consulted with Board Staff and intervenor colleagues as appropriate on issues of common interest.

2.0 SUBMISSIONS

2.1 General

The QMA recognizes the fact that Ontario’s energy sector is evolving quickly and is reassured that the Ontario Energy Board’s regulatory oversight of electricity distributors, including Hydro One, is to carefully balance the interests of customers and distributors to ensure there is “value for money” that electricity customers pay in rates.¹

QMA members are actively engaged in applying energy efficiency initiatives and technology innovation and improvements in their manufacturing facilities to constantly reduce waste, improve production efficiency and cost effectiveness. Digital control systems, the use of artificial intelligence and robotics, for example, are being applied to equipment and facilities and they all rely on reliable electricity to operate.

The QMA recognizes the importance of having to work closely with Hydro One to ensure the distribution network, power quality and reliability in the Quinte area is “first class”. Recognition by Hydro One in its Application evidence that it is facing system reliability and aging assets (such as transformers and conductor carrying wood poles) issues now and going forward is a concern for the QMA. The Association recognizes this is an on-going cost challenge for Hydro One that must be addressed. The QMA wants a stronger dialogue with

¹ OEB Report – *Renewed Regulatory Framework for Electricity Distributors*, October 2012

Hydro One to consider forward planning issues that could have a direct impact on individual business decisions. Improved customer-Hydro One interaction is vital for expanding business and attracting new business. The QMA strongly believes that electricity “issues” should not become a reason that drives business away from the Quinte region.

The Ontario Energy Board in the issuance of Procedural Order No. 8 in this proceeding, stated that it considers regulatory consistency to be an important factor in making its determinations in establishing just and reasonable rates.² This is also an important consideration for QMA members who are looking for certainty in electricity costs for current and forward business planning purposes and rely on that level of regulatory oversight. Although the QMA has not participated in previous Hydro One distribution rate filings, we believe Hydro One has been clear in its evidence and established through testimony given in the cross-examination of its witness panels, that it has made and will continue to make significant improvements in its distribution business operations as per OEB requirements compared to previous rate filings. On that basis, the QMA is in general support of Hydro One’s five-year Custom IR approach and the regulatory foundation established by the OEB upon which it has been developed.³

The QMA recognises the fact that the Ontario government partially privatized Hydro One Networks Inc. in 2015 creating a new business structure for the delivery of electricity distribution services in the province. From the evidence presented, Hydro One’s Board of Directors and the corporation’s senior leadership have initiated the steps necessary to transition Ontario’s largest distribution utility on to an enterprise path that is more commercially oriented to drive the changes necessary to make it more efficient and productive to achieve the range of outcomes it’s committing to.⁴ The QMA believes this is a positive move on the part of Hydro One’s Board, but is concerned that the ongoing need

² Although Procedural Order No. 8 addresses the issue of pole attachments, the Board’s consideration of “regulatory consistency” between decisions is considered important by the QMA.

³ Argument in Chief, pg. 10-11

⁴ The Board of Directors responsible for the oversight of the Application has been retired by the Government of Ontario with a new Board to be appointed in due course.

for investment in maintaining and upgrading its extensive asset base stretched across Ontario will challenge its ability to improve productivity and reliability and yet minimize rate impacts on its distribution customers over the five year term contemplated in the Application.

During the process of developing the Application, Hydro One's Board of Directors considered three possible five-year investment plans (known as plans "A", "B" and "C") for the utility's distribution system. The Board of Directors approved a 5-year Custom IR plan for its distribution system investment strategy known as the "Modified Plan B". Hydro One stated that this outcome addresses concerns raised through its customer engagement process and reflects the desire of the utility be more responsive to the demands of consumers to minimize rate increases over the five years. It will achieve this through improvements in corporate efficiency, productivity, effectiveness, reducing unnecessary capital expenditures while maintaining system assets and reliability.⁵ The QMA supports the aggressiveness of Hydro One's plan to sustain its distribution assets while minimizing deterioration and committing to make it work as explained by the Asset Management Panel during cross-examination.⁶ The QMA believes a strong corporate focus by Hydro One on continuous improvement and financial accountability are key drivers necessary to being a more commercially oriented distribution utility.

The QMA takes no position in respect to Hydro One's acquisition of the acquired utilities that are to be integrated as part of its distribution network in 2021.⁷

3.0 SPECIFIC ISSUES

3.1 Issue 2: Has Hydro One adequately responded to the customer concerns expressed in the Community Meetings held for this application?

⁵ Argument in Chief, pg.8, pg. 21, pg. 43

⁶ Argument in Chief, pg. 123-126

⁷ The local distribution companies that are identified as the acquired utilities in the application are: Norfolk Power Distribution Inc., Haldimand County Hydro Inc., and Woodstock Hydro Services Inc.

QMA members attended the OEB hosted community meeting held on June 19, 2017 in Napanee, Ontario. The QMA views such meetings as a form of pre-submission (of an application) consultation and considers them helpful and informative on a broad scale. Significant concerns such as the high cost of power (collectively generation, transmission, distribution and the global adjustment) in Ontario and the high levels of executive compensation were raised at this meeting.⁸

Concerns expressed throughout the community meetings particularly with respect to the high cost of power in Ontario and its impact on business and the high salaries and benefits (compensation) paid to Hydro One employees when compared to the compensation paid to employees other industries in the province rings true with QMA members. The QMA noted through Hydro One's evidence and the testimony given during the oral portion of the hearing that these serious concerns have been recognized at the highest levels of the corporation and it has responded accordingly through the development of Custom IR process.

The QMA supports the Board's community meeting initiative with Hydro One to assist the utility in informing and improving the development of its Application. The QMA notes that not all community meetings were well attended. This would suggest that not all customer classes were represented at those meetings as well. The QMA submits that distribution utilities such as Hydro One should improve efforts to attract a good cross-section of community representation to provide input from all customer classes served by the utility in key economic regions and sub-regions of the province such as the Bay of Quinte area.

3.2 Issue 6: Does Hydro One's First Nation and Métis Strategy sufficiently address the unique rights and concerns of Indigenous customers with respect to Hydro One's distribution service?

While this issue is not of specific concern to the QMA in this proceeding, the Association recognizes the importance of the Anwaatin – Hydro One settlement agreement that was

⁸ OEB Staff Summary of Community Meetings, EB-2017-0049, September 7, 2017

presented on day five (June 18, 2018) of the oral hearing and offers the following comments that the Board may find helpful in its deliberations.⁹

Local system reliability issues impact not only local communities as described in the settlement agreement but can also affect manufacturing facilities. System reliability is a concern from time to time for certain QMA members and consideration of alternative or complimentary supply options such as distributed energy resources (“DER”) is being explored. The QMA supports the DER Pilot Project contemplated in the settlement agreement as an opportunity to learn and be informed about the value and effectiveness of DER facilities under certain circumstances and conditions.¹⁰

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

The QMA is concerned with one productivity related matter under this issue and agrees with Board Staff’s position that the size of Hydro One’s licensed service territory across Ontario and its related customer density may misrepresent the proper benchmarking of Hydro One’s distribution assets against its peers.¹¹

The QMA considers benchmarking a valuable analytical tool for determining how well a business or business activity is performing on a range of parameters internally and externally. It is essential that the benchmarking parameters used are as accurate as possible.

Consistent with the need for better benchmarking and utility performance improvement identified in by the OEB in previous applications, Hydro One has determined its customer density based on the number of customers it serves per square kilometer across its licensed service territory. The QMA observes that the vast landmass of northwestern Ontario which makes-up the largest land portion of the province of Ontario and is included in the service

⁹ Argument in Chief, pg. 28

¹⁰ Undertaking J11.4

¹¹ Distribution licence for Hydro One Networks Inc. – ED-2003-0043

territory of Hydro One's distribution licence, is largely unserved, uninhabited wilderness, sparsely populated and scattered with small and often remote communities. The QMA agrees with Board Staff on this matter and is of the opinion that the areal extent of the Hydro One's service territory is unlike any other utility in its benchmarking peer group and effectively makes it an "outlier" when comparing customer densities. Consequently, Hydro One's assets appear to have a very low density of connected customers per distribution line length when compared to the geographic size of its licensed service territory and urban service territories with higher levels of connected customer density per distribution line.¹²

If good cost benchmarking is dependent on a metric that correctly accounts for connected customer density, then this number should be as accurate and reflective as possible. The QMA submits that improving the accuracy and characteristics of Hydro One's more remote, non-urban, customer density on a connected customer per distribution line kilometer number rather than on a square kilometer basis may better inform the benchmarking exercise and more accurately reflect the true cost of distribution service in sparsely populated areas that needs to be recovered in rates.

3.4 Issue 15: Is the proposed Earnings/Sharing mechanism appropriate?

The QMA agrees with Hydro One's proposal to split on with its customers any excess earnings it achieves over its allowed return on equity each year of the Custom IR plan on a 50:50 basis through the proposed Earnings/Sharing Mechanism ("ECM").¹³ Considering Hydro One is moving towards a becoming more commercially oriented enterprise as a partially-owned crown corporation, the sharing mechanism is a fair and reasonable approach that incents the utility to carefully manage its business and hit its stated financial targets for the benefit of both its shareholders and its customers. The QMA expects that

¹² Ex. B1-1-1 DSP S2.2 pg. 3

¹³ Argument in Chief, pg. 42

Hydro One's improved benchmarking techniques and resulting efficiency gains across the enterprise as a result of good business practice will be reflected as an ECM benefit.

3.5 Issue 17: Does the application adequately incorporate and reflect the four outcomes identified in the Rate Handbook: customer focus, operational effectiveness, public policy responsiveness, and financial performance?

In addition to the issue of "community engagement", the QMA is particularly concerned with the issue of "customer focus". The Association views any interaction between Hydro One and its members whether it is through broad-based community engagement or one-on-one meetings, customer focus is critical for improving business to business relationships, addressing issues and planning for the future. QMA members have a good working relationship with the local Hydro One distribution system staff in the Quinte region. Typically, interaction with Hydro One is almost exclusively the result of a power supply issue that needs to be addressed. Hydro One's staff are responsive and professional.

As noted above, our manufacturers are installing and using increasingly sophisticated and technically advanced processing and assembly equipment in their plants to maintain competitive advantage in the market. The requirement for very "clean", stable and reliable power is increasingly critical for the operational efficiency and productivity of these plants. The QMA is concerned that aging distribution assets in the Quinte region may put our manufacturers at risk of loss of supply and shutdown. While the QMA is encouraged by Hydro One's evidence that it is focusing on getting better information on customer needs and preferences regarding its distribution services as it implements "aggressive" efforts to improve operational effectiveness and drive improvements in productivity, it is concerned that productivity savings not impair appropriate capital investments needed to modernize and maintain Hydro One's distribution network in the Quinte region for the reasons mentioned above. The QMA is of the view that not all distribution system upgrades will necessarily be driven by load growth.

The QMA supports Hydro One’s “new” approach to customer engagement to become a more commercially focused corporation. Mr. Pugliese in his testimony during the oral portion of the hearing stated that feedback from Hydro One customers “informed” the Application and how the utility conducts business.¹⁴

While the QMA recognizes the large and diversified customer base Hydro One serves across Ontario and the challenge in getting valuable customer feedback. Hydro One used the polling firm IPSOS to engage customers in an “extensive early consultation process” and help inform the Distribution System Plan development process¹⁵ The QMA considers this a positive step forward, but QMA members were not consulted through the IPSOS process and remain concerned that true customer engagement with its manufacturers has yet to be achieved.

As the utility moves to become more commercially oriented with a stronger focus on customer needs and preferences the QMA submits that Hydro One must make a stronger effort to engage manufacturers in its benchmarking and local system planning work to plan for the future development and avoid unforeseen or unintentional consequences to facilities that rely heavily on Hydro Ones distribution services. The QMA submits that system reliability cannot be compromised to the point where it could negatively impact manufacturers. While there can always be opportunities to enhance system reliability in the Quinte region, QMA members, are generally pleased with the current level of reliability and excellent customer service provided by Hydro One’s field operations (as noted earlier) and support staff to help ensure manufacturing facilities remain “on-line”. However, members are concerned that certain local system planning and other potential operational issues that could impact manufacturing plant expansion, for example, may not be identified because of weak customer feedback.

¹⁴ Argument in Chief pg. 43

¹⁵ *Ibid*, Pg. 43

QMA member manufacturers rely on regular customer feedback to help improve products and services, identify market opportunities, threats and challenges. The QMA is encouraged by Mr. Pugilese's comments during cross-examination that Hydro One has undertaken a lot of engagement work with residential customer, but there is much more work to do with their large accounts, commercial and industrial customers and small business customers; and that work is underway.¹⁶

The QMA submits that improved customer engagement and a focus on customer needs with manufacturers in the Bay of Quinte sub-economic region is becoming increasingly important. This is the opportunity for Hydro One to engage with manufacturers to better understand needs and share information on local distribution issues and potential capital investment in distribution assets. By extension, this assists the region in business attraction, job creation and business retention. The QMA encourages the Energy Board to ensure customer engagement and customer focus is a cornerstone of the Hydro One five-year plan.

3.6 Issue 23: Was the customer consultation adequate and does the Distribution System Plan adequately address customer needs and preferences

As noted under Issue 17 above, The QMA is not aware that any of its members were part of the customer engagement process developed by IPSOS for the Distribution System Plan ("DSP"). The QMA takes no issue with the DSP per se but recognizes that the "customer focus" outcome of the RRF that is embedded as a Hydro One business objective, needs to be more inclusive in terms of customer engagement to get better customer input to the plan as it is updated. Board Staff recognized a similar concern in their submissions¹⁷

Further, the QMA recognizes that Hydro One's third-party reviewer of the DSP, AESI Inc. indicated that it was developed appropriately and consistent with the "best practices"

¹⁶ Transcript Day 4, pg. 178-186

¹⁷ Board Staff Submission, pg. 60-62

approach.¹⁸ However, the active engagement of manufacturers and related industries that operate in close proximity to one another such as the Quinte region would have better informed the DSP and help minimize potential risk of power quality or reliability issues going forward. The QMA submits that Hydro One should be strongly encouraged to expand its “best practices” efforts to improve communications efforts with manufacturers, particularly in developing areas, to better inform the updating process for the DSP and be reflected in Hydro One’s corporate scorecard reporting system.

3.7 Issue 29: Are the proposed capital expenditures resulting from the Distribution System Plan appropriate, and have they been adequately planned and paced?

The QMA has a comment on this issue related to the matter of “redirection” and reprioritization of projects and programs. That activity was explored during the cross-examination of with Hydro One’s Asset Management Panel during the oral portion of the hearing.¹⁹ It concerns the replacement of PCB contaminated equipment and pole mounted transformers in particular. In its Argument in Chief, Hydro One states “... [it] has significant asset needs that necessitate certain spending so that Hydro One can maintain the condition of its assets and not defer problems to future rate payers.”²⁰ The QMA considers “redirection” of resources a normal business option to address certain unexpected or unanticipated events, for example. The QMA is concerned that given the federally mandated obligation to replace PCB contaminated equipment by December 31, 2025 there may be the potential for a shortfall of funds available in 2022 that may cause Hydro One to seek an increase in rates to address the shortfall and replace the equipment.²¹ The QMA is aware that PCB industrial contamination and clean-up has been an issue of concern in Ontario for many years. Although there is Hydro One senior management oversight of redirection activities, the Association is concerned that funds specifically allocated by Hydro One in its Application for the purpose of PCB contaminated equipment replacement

¹⁸ Argument in Chief, pg. 16

¹⁹ Argument in Chief, pg. 93-95

²⁰ Argument in Chief, pg. 87

²¹ Ex. B1-1-1, DSP S2.3, pg. 45-50

for each year of the capital investment plan will continue to be redirected to other priorities. The QMA is in general support of Board Staff's position on the matter of redirection of capital expenditures and Hydro One's ability to manage the same appropriately, but cautions that the capital expenditures necessary to address PCB contaminated equipment during the forecast years should not be put in jeopardy and be left to ratepayers to unfairly fund beyond 2022.²²

3.8 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)?

Although the matter of executive compensation at Hydro One is excluded as an issue in this proceeding, the level of compensation costs and compensation increase at the non-executive levels at Hydro One is a concern and will remain a concern of QMA members. The QMA recognizes that Hydro One is a unique distribution utility when compared to its peers which are often identified as U.S based utilities. Its historic roots as fully integrated part of the former Ontario Hydro which operated as a self-regulating crown corporation responsible for regulating local distribution services in Ontario and then later as Hydro One, a provincially owned crown corporation regulated by the OEB and now as a partially privatized corporation still serving most of the geographic area of Ontario. Even though Hydro One has been restructured, the QMA believes that the utility will continue to have certain legacy challenges that need to be addressed (such as compensation issues, a highly unionized business and partial provincial ownership) as it shifts to a more commercialized enterprise. In doing the QMA believes Hydro One must demonstrate "value for money" as triggered by the OEB's renewed regulatory framework.

The Mercer Canada study that was undertaken by Hydro One shows that its compensation levels exceed the market median for its peers.²³ The evidence shows that this tends to be

²² Board Staff Submissions pg. 75

²³ Mercer Canada Study – Compensation Cost Benchmarking Study, Hydro One Networks Inc., 2017

a recurring issue that has been challenging to address by Hydro One's management. The QMA is of the opinion that labour and associated compensation costs have to be managed within the business revenue envelope that's available in any given year for a commercially driven enterprise. The QMA recognizes a critical difference in corporate scale between our manufacturers who have to deal with their own internal compensation issues that can be impacted by internationally volatile competitive markets and Hydro One's Ontario customer "market". Hydro One is in the fortunate position of having a long-standing pool of "captive" distribution customers across Ontario who pay rates (albeit regulated) every month, year over year to cover the costs of distribution service, because there is no real market alternative for the supply of that service. With all things considered, including any regulatory adjustments, this suggests a high level of certainty in Hydro One's revenue stream on an annual basis. Based on the evidence presented, the QMA believes Hydro One leadership is concerned that compensation levels are out-of-step with industry peers (as shown in the Mercer Canada Study) and must be brought in-line with the market median for a distribution utility of its type. The QMA submits that it is important that the OEB require Hydro One to make every effort to bring compensation levels in line with its benchmarked peers within a set timeframe.

3.9 Issue 45: Are the proposed revenues for 2018 – 2022 appropriate?

The QMA offers the following comment on this issue.

From time to time and under certain circumstances QMA members may take advantage of other specific distribution/miscellaneous services offered by Hydro One to assist with changes or adjustments in manufacturing processes or procedures.²⁴ These are typically one-off events (e.g. metering change-outs or sub-metering) that are customer specific and should be charged for accordingly. The QMA has reviewed Hydro One's proposed service charges and the related time study that was undertaken to determine the accuracy of the charges. The QMA is of the general opinion that the charges are appropriate and that there

²⁴ Argument in Chief, pg. 141-144

should be no cross-subsidization between rate classes for these services, and the focus should be on a user-pay basis. Further, the QMA agrees with Board Staff that improved customer engagement (as discussed above) by Hydro One in advance of developing new or increased charges would be fair and reflect good business practice.²⁵

4.0 COSTS

The Quinte Manufacturers Association requests that it be granted 100% of its reasonably incurred costs for its intervention and participation in this proceeding.

All of which is respectfully submitted, August 10, 2018

by the

Quinte Manufacturers Association

²⁵ Ibid, pg. 143