G-Staff-6

Reference: IRR G-Staff-4

Preamble:

In G-Staff-4, OEB staff requested that Alectra Utilities compare its proposed method for calculating the return component of changes in capitalization policy to the return component methodology that has historically been applied by the OEB to balances in Account 1575 and 1576. Specifically, OEB staff stated the following in G-Staff-4 f):

> **Aside from the distinction stated in the preamble (and the inclusion of PILs impacts), is there any other rationale that Alectra Utilities can provide to support the OEB varying its calculation methodology previously used for the impacts of changes in accounting policy between rebasing years?**

In response, Alectra Utilities asserted that its method of calculating the return component of changes in accounting policies is consistent with the Account 1575 and 1576 method, stating:

> **Alectra Utilities' calculation method of return on rate base is consistent with the calculation of the return used for Accounts 1575 and 1576. For the calculation of the return please see Alectra Utilities' Capitalization Policy Impact Model filed in response to G-Staff-3.**

However, in G-Staff-4 c), OEB staff asked Alectra Utilities to confirm that its calculation method results in a collection from ratepayers in cases where accounting policy changes result in increases to rate base, while the Account 1575/1576 method would result in a refund to customers. Alectra Utilities confirmed these circumstances in their response.

Please reconcile the two positions above by directly confirming the following differences between Alectra Utilities' method and the 1575/1576 method for return on capital (if any of the below is not confirmed, please provide a detailed explanation):

a) **The return on capital calculation under Account 1575/1576 results in amounts being returned to ratepayers when there is an increase to rate base, while Alectra Utilities' method results in a collection from ratepayers for that component. Conversely, the return on capital calculation under Account 1575/1576 results in amounts being collected from ratepayers when there is a decrease to rate base, while Alectra Utilities' method results in a collection from ratepayers for that component.**

b) **The 1575/1576 method is non-compounding. Specifically, it takes the cumulative PPE (property, plant, and equipment) difference since the change in accounting policy took place and calculates the return component as: the <u>cumulative PPE difference</u>, multiplied by the weighted average cost of capital, multiplied by the number of years that the associated rate rider will be in effect for.**

Alectra Utilities method is compounding. Specifically, it takes the closing PPE difference at the end of <u>each year</u> since the change in accounting policy took place and calculates the return component as the closing PPE difference <u>at the end of that year</u> multiplied by the weighted average cost of capital.

Response:

a) and b) Alectra Utilities initially provided a forecast of the impact of the capitalization policy change in response to Technical Conference undertaking JT.Staff-7, filed December 15, 2017 in Alectra Utilities' 2018 EDR Application (EB-2017-0024). In response to JT.Staff-7, Alectra Utilities stated that to capture the net impact of the capitalization policy change, the change should include the impact of the following items:

- The actual impact on OM&A expenditures in each year following the change in capitalization policy until rebasing;
- The actual impact on depreciation expense over the life of the underlying assets as a result of the increase/decrease in capitalization costs;
- The impact on income tax or PILs; and
- The annual return on the cumulative impact from the annual change in capitalization

Alectra Utilities further identified that the increase in capitalized costs for the Enersource and Horizon Utilities rate zones results in a corresponding reduction in OM&A expenditures and an increase in depreciation expense over the life of the underlying assets. The decrease in capitalized costs for the Brampton rate zone results in a corresponding increase in OM&A expenditures and a decrease in depreciation expense over the life of the underlying assets. **Further, the total impact must be <u>offset</u> by the annual return on the cumulative capital that can only be added to a distributor's rate base at rebasing [emphasis added].**

In the OEB's Decision and Partial Accounting Order, dated December 20, 2017 (EB-2017-0024), the OEB identified at p. 2, that *"Alectra Utilities' proposal would record the impact resulting from the change to the capitalization policy for the following:*

- *OM&A expenditures in each year*
- *depreciation expense over the life of the underlying assets;*
- *income tax or PILs for the amount paid to taxation authorities*
- *the annual return on the cumulative capital"*

At p. 3 of the OEB's Findings, the OEB stated *"The three new accounts will record the difference between the revenue requirement calculated using the pre-merger capitalization policies and the revenue requirement calculated with the new capitalization policy. The revenue requirement will be calculated each year based on actual costs for OM&A, depreciation expense, income tax or PILs, and return on capital (debt and equity). This approach will result in the actual financial consequences of the change to the capitalization policy being recorded in the new accounts."* The OEB went on to state that *"Alectra Utilities shall maintain records to show its calculations for the revenue requirement for each rate zone to at least the level of detail provided in Table 1 of the undertaking JT.Staff-7."*

OEB Staff has asked Alectra Utilities to reconcile its calculation of the return component and specifically the calculation of the return on the cumulative Property, Plant and Equipment ("PP&E") difference.

As demonstrated in Alectra Utilities' calculation of the net impact of the capitalization policy change, as provided in response to the first round of capitalization policy interrogatories (G-Staff-3), the purpose of the calculation is to ensure that the impact of the capitalization policy change is not recovered from customers twice in rates; once through OM&A and then through capital. To ensure the impact results in a fair, balanced and principled approach, Alectra Utilities' calculation ensures the full impact to OM&A is refunded (dollar for dollar) to customers. This is partially offset by increased depreciation expense which is not being recovered in rates; a return on rate base that Alectra Utilities is not earning during the rebasing deferral period as this capital cannot be added to rate base; and a minimal impact to PILs.

If the capitalization policy change would have been in place at the time of each legacy utilities' rebasing applications, each legacy utility would have been earning a higher return on rate base and OM&A would have been lower. As a result, Alectra Utilities should (consistent with its proposal) refund the OM&A impact to customers. In order to ensure a fair and balanced approach to the calculation of the impact, the calculation must also account for the return that is not added to rate base in each year. Not only is Alectra Utilities not able to include the lost return of the additional capital in each incremental year, but the return in a prior year is also not earned in each subsequent year. Consequently, the impact of the return must be calculated on the cumulative capital. This is consistent with the itemization of the impact as provided in response to JT.Staff-7.

G-Staff-7

Reference: IRR G-Staff-4
Reference: Alectra_IRR_G-Staff-3_Attach 1_Capitalization Policy Impact Model_20191007

Preamble:

In G-Staff-4, parts h) and i), OEB staff asked Alectra Utilities to prepare the disposition amounts for the Enersource (ERZ) and Brampton (BRZ) rate zones using the 1575/1576 method (ERZ and BRZ being the rate zones that are eligible for disposition in this proceeding). OEB staff also asked Alectra Utilities to restate its table that summarizes the total impacts of the change in accounting policy (Table 20 of Exhibit 2, Tab 1, Schedule 5) using the 1575/1576 method for calculating return on capital.

In response, Alectra Utilities asserted that its method is consistent with the 1575/1576 method and directed OEB staff to its Capitalization Policy Impact Model, which is the supporting document for the Alectra Utilities' method.

Similar to G-Staff-6, OEB staff notes key differences in the 1575/1576 method versus Alectra Utilities' method. OEB staff has prepared the accounting policy impacts using the 1575/1576 method for the record in this proceeding and provides them below as Figures 1 to 7. Figures 1 to 5 show the cumulative impact for all five rate zones assuming disposition occurs upon rebasing, while Figures 6 to 7 calculate the amounts eligible for disposition under this method for the 2017-2018 impacts in the Enersource and Brampton Rate Zones assuming disposition of the accounts in this proceeding.

OEB staff has used tab 2-EC from the Chapter 2 Appendices for 2019 cost of service applications.[1] The changes and assumptions made by OEB staff in these calculations are:

- **All references to different reporting bases (IFRS/CGAAP/etc.) have been removed.**
- **The years in each table have been updated to coincide with the affected periods for each rate zone.**
- **The most recent weighted average cost of capital for each rate zone has been used, as provided in Alectra Utilities' Capitalization Policy Impact Model.**
- **The capital additions and depreciation impacts for each rate zone have been populated under the revised accounting policy rows, per Alectra Utilities' Capitalization Policy Impact Model.**
- **A 1-year disposition period is assumed.**
- **For comparative purposes to Alectra Utilities' Capitalization Policy Impact Model, the Horizon Rate Zone has been populated for 2017-2019 and the Powerstream Rate Zone for 2017-2026 has been included as well.**

[1] Any similar 1575/1576 tabs from the Chapter 2 Appendices since 2014 would produce identical results.

a) **Please confirm that OEB staff has prepared the capitalization policy impacts, using the 1576 method, with factual accuracy and in accordance with the OEB's current methodology. If Alectra Utilities believes that OEB staff has made an error in applying the 1576 methodology for any of Figures 1 to 7 below, please explain in detail and provide a revised copy of the table(s), stating any changes that were made and why they were made.**

Figure 1
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Horizon Rate Zone

	2017 Actual $	2018 Actual $	2019 Forecast $	2020 Forecast $	2021 Forecast $	2022 Forecast $	2023 Forecast $	2024 Forecast $	2025 Forecast $	2026 Forecast $	2027 Rebasing Year Forecast $
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	5,263,566	10,240,272	16,268,230	21,808,545	26,944,785	31,860,631	35,580,540	40,407,103	45,084,537	
Net Additions - Note 3	5,398,529	5,242,737	6,455,375	6,120,749	5,863,256	5,787,550	4,709,348	5,965,129	5,965,129	5,965,129	
Net Depreciation (amounts should be negative) - Note 3	(134,963)	(266,032)	(427,416)	(580,435)	(727,016)	(871,705)	(989,439)	(1,138,567)	(1,287,695)	(1,362,259)	
Closing net PP&E (2)	5,263,566	10,240,272	16,268,230	21,808,545	26,944,785	31,860,631	35,580,540	40,407,103	45,084,537	49,687,407	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	(5,263,566)	(10,240,272)	(16,268,230)	(21,808,545)	(26,944,785)	(31,860,631)	(35,580,540)	(40,407,103)	(45,084,537)	(49,687,407)	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**(49,687,407)**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**(2,881,472)**
Amount included in Deferral and Variance Account Rate Rider Calculation	**(52,568,880)**

WACC	5.80%
# of years of rate rider disposition period	1

Notes:
1 Return on rate base associated with Account 1576 balance is calculated as:
the variance account ending balance as of 2026 x WACC x # of years of rate rider disposition period
* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.
2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.
3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Figure 2
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Enersource Rate Zone

	2017 Actual $	2018 Actual $	2019 Forecast $	2020 Forecast $	2021 Forecast $	2022 Forecast $	2023 Forecast $	2024 Forecast $	2025 Forecast $	2026 Forecast $	2027 Rebasing Year Forecast $
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	1,819,390	3,441,469	5,111,832	6,678,668	8,478,907	10,399,041	12,295,232	14,605,254	16,847,329	
Net Additions - Note 3	1,866,041	1,711,518	1,804,925	1,745,024	2,029,155	2,204,155	2,236,114	2,717,893	2,717,893	2,717,893	
Net Depreciation (amounts should be negative) - Note 3	(46,651)	(89,439)	(134,562)	(178,188)	(228,917)	(284,020)	(339,923)	(407,871)	(475,818)	(509,792)	
Closing net PP&E (2)	1,819,390	3,441,469	5,111,832	6,678,668	8,478,907	10,399,041	12,295,232	14,605,254	16,847,329	19,055,431	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	(1,819,390)	(3,441,469)	(5,111,832)	(6,678,668)	(8,478,907)	(10,399,041)	(12,295,232)	(14,605,254)	(16,847,329)	(19,055,431)	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**(19,055,431)**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**(1,239,670)**
Amount included in Deferral and Variance Account Rate Rider Calculation	**(20,295,101)**

Notes:

1 Return on rate base associated with Account 1576 balance is calculated as:	**WACC**	6.51%
the variance account ending balance as of 2026 x WACC x # of years of rate rider disposition period	**# of years of rate rider disposition period**	1

* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.

2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.

3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Figure 3
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Brampton Rate Zone

	2017 Actual $	2018 Actual $	2019 Forecast $	2020 Forecast $	2021 Forecast $	2022 Forecast $	2023 Forecast $	2024 Forecast $	2025 Forecast $	2026 Forecast $	2027 Rebasing Year Forecast $
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	(1,784,769)	(3,308,453)	(5,494,280)	(7,843,405)	(9,859,667)	(12,163,296)	(14,358,525)	(16,531,496)	(18,638,600)	
Net Additions - Note 3	(1,830,532)	(1,609,690)	(2,330,085)	(2,557,315)	(2,281,490)	(2,634,725)	(2,591,103)	(2,634,712)	(2,634,712)	(2,634,712)	
Net Depreciation (amounts should be negative) - Note 3	45,763	86,006	144,258	208,191	265,228	331,096	395,873	461,741	527,609	560,543	
Closing net PP&E (2)	(1,784,769)	(3,308,453)	(5,494,280)	(7,843,405)	(9,859,667)	(12,163,296)	(14,358,525)	(16,531,496)	(18,638,600)	(20,712,769)	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	1,784,769	3,308,453	5,494,280	7,843,405	9,859,667	12,163,296	14,358,525	16,531,496	18,638,600	20,712,769	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**20,712,769**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**1,492,479**
Amount included in Deferral and Variance Account Rate Rider Calculation	**22,205,249**

Notes:

1 Return on rate base associated with Account 1576 balance is calculated as:	**WACC**	7.21%
the variance account ending balance as of 2026 x WACC x # of years of rate rider disposition period	**# of years of rate rider disposition period**	1

* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.

2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.

3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Figure 4
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Powerstream Rate Zone

	2017 Actual	2018 Actual	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	2026 Forecast	2027 Rebasing Year Forecast
	$	$	$	$	$	$	$	$	$	$	$
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	188,819	583,442	828,819	1,101,980	1,365,065	1,616,173	1,927,522	2,206,042	2,476,053	
Net Additions - Note 3	193,660	409,708	267,139	302,487	299,907	295,314	364,670	340,351	340,351	340,351	
Net Depreciation (amounts should be negative) - Note 3	(4,842)	(15,084)	(21,763)	(29,325)	(36,823)	(44,205)	(53,322)	(61,831)	(70,340)	(74,594)	
Closing net PP&E (2)	188,819	583,442	828,819	1,101,980	1,365,065	1,616,173	1,927,522	2,206,042	2,476,053	2,741,810	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	(188,819)	(583,442)	(828,819)	(1,101,980)	(1,365,065)	(1,616,173)	(1,927,522)	(2,206,042)	(2,476,053)	(2,741,810)	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**(2,741,810)**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**(157,797)**
Amount included in Deferral and Variance Account Rate Rider Calculation	**(2,899,607)**

WACC	5.76%
# of years of rate rider disposition period	1

Notes:
1 Return on rate base associated with Account 1576 balance is calculated as:
the variance account ending balance as of 2026 x WACC x # of years of rate rider disposition period
* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.
2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.
3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Figure 5
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Guelph Rate Zone

	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	2026 Forecast	2027 Forecast	2028 Forecast	2029 Rebasing Year Forecast
	$	$	$	$	$	$	$	$	$	$	$
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	573,291	1,180,786	1,803,839	2,409,546	2,939,386	3,537,573	4,118,387	4,681,827	5,227,893	
Net Additions - Note 3	587,990	638,149	670,468	669,869	609,233	694,954	694,954	694,954	694,954	694,954	
Net Depreciation (amounts should be negative) - Note 3	(14,700)	(30,653)	(47,415)	(64,162)	(79,393)	(96,767)	(114,140)	(131,514)	(148,888)	(157,575)	
Closing net PP&E (2)	573,291	1,180,786	1,803,839	2,409,546	2,939,386	3,537,573	4,118,387	4,681,827	5,227,893	5,765,272	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	(573,291)	(1,180,786)	(1,803,839)	(2,409,546)	(2,939,386)	(3,537,573)	(4,118,387)	(4,681,827)	(5,227,893)	(5,765,272)	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**(5,765,272)**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**(374,258)**
Amount included in Deferral and Variance Account Rate Rider Calculation	**(6,139,530)**

WACC	6.49%
# of years of rate rider disposition period	1

Notes:
1 Return on rate base associated with Account 1576 balance is calculated as:
the variance account ending balance as of 2028 x WACC x # of years of rate rider disposition period
* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.
2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.
3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Figure 6
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Enersource Rate Zone

	2017 Actual	2018 Actual	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	2026 Forecast	2027 Rebasing Year Forecast
	$	$	$	$	$	$	$	$	$	$	$
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	1,819,390	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	
Net Additions - Note 3	1,866,041	1,711,518									
Net Depreciation (amounts should be negative) - Note 3	(46,651)	(89,439)									
Closing net PP&E (2)	1,819,390	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	3,441,469	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	(1,819,390)	(3,441,469)	(3,441,469)	(3,441,469)	(3,441,469)	(3,441,469)	(3,441,469)	(3,441,469)	(3,441,469)	(3,441,469)	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**(3,441,469)**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**(223,888)**
Amount included in Deferral and Variance Account Rate Rider Calculation	**(3,665,357)**

WACC	6.51%
# of years of rate rider disposition period	1

Notes:
1 Return on rate base associated with Account 1576 balance is calculated as:
the variance account ending balance as of 2018 x WACC x # of years of rate rider disposition period
* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.
2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.
3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Figure 7
Appendix 2-EC
Account 1576 - Accounting Changes between Rebasing Years
Brampton Rate Zone

	2017 Actual	2018 Actual	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	2026 Forecast	2027 Rebasing Year Forecast
	$	$	$	$	$	$	$	$	$	$	$
PP&E Values under former Accounting Policy											
Opening net PP&E	0	0	0	0	0	0	0	0	0	0	
Net Additions - Note 3											
Net Depreciation (amounts should be negative) - Note 3											
Closing net PP&E (1)	0	0	0	0	0	0	0	0	0	0	
PP&E Values under revised Accounting Policy											
Opening net PP&E	0	(1,784,769)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	
Net Additions - Note 3	(1,830,532)	(1,609,690)									
Net Depreciation (amounts should be negative) - Note 3	45,763	86,006									
Closing net PP&E (2)	(1,784,769)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	(3,308,453)	
Difference in Closing net PP&E, former Accounting Policy vs revised Accounting Policy	1,784,769	3,308,453	3,308,453	3,308,453	3,308,453	3,308,453	3,308,453	3,308,453	3,308,453	3,308,453	

Effect on Deferral and Variance Account Rate Riders	
Closing balance in Account 1576	**3,308,453**
Return on Rate Base Associated with Account 1576 balance at WACC - Note 1	**238,394**
Amount included in Deferral and Variance Account Rate Rider Calculation	**3,546,847**

WACC	7.21%
# of years of rate rider disposition period	1

Notes:
1 Return on rate base associated with Account 1576 balance is calculated as:
the variance account ending balance as of 2018 x WACC x # of years of rate rider disposition period
* Please note that the calculation should be adjusted once WACC is updated and finalized in the rate application.
2 Account 1576 is cleared by including the total balance in the deferral and variance account rate rider calculation.
3 Net additions are additions net of disposals; Net depreciation is additions to depreciation net of disposals.

Response:

a) Alectra Utilities does not agree with OEB staff's presentation of the impact of the capitalization policy change in Figures 1 through 5 above. As provided in response to G-Staff-6, and consistent with the OEB's Decision and Partial Accounting Order in EB-2017-0024, dated December 20, 2017, "*The revenue requirement will be calculated each year based on actual costs for OM&A, depreciation expense, income tax or PILs, and return on capital (debt and equity). This approach will result in the actual financial consequences of the change to the capitalization policy being recorded in the new accounts.*"

OEB staff's figures do not include the PILs impact; and do not accurately present the impact of the return on rate base. For example, in Figure 2, OEB staff presents the return as a refund to customers and does not account for the cumulative impact of the return as identified by Alectra Utilities. First, it is fundamentally incorrect to refund a return to customers that Alectra Utilities has not received from customers. As provided in response to G-Staff-6, Alectra Utilities is **not** able to add the additional capitalized balances to rate base during the rebasing deferral period and is **not** currently earning a return on this capital. It is therefore, improbable that Alectra Utilities can refund to customers an amount it has never received. Alectra Utilities has calculated a refund of the full OM&A impact to customers, only partially offset by depreciation, PILs and a return that can only be added to rate base upon rebasing.

Alectra Utilities refers OEB staff to Attachment 1 of G-Staff-3 from the first round of capitalization policy interrogatories, for the complete and detailed calculation of the impact of the capitalization policy change.

G-Staff-8

Reference: IRR G-Staff-4

Preamble:

In G-Staff-4 g), OEB staff asked Alectra Utilities: in the event that the OEB decides to apply the 1575/1576 methodology for the calculation of the capitalization policy impacts, what rate rider disposition period would it select for those balances? In response, Alectra Utilities referred OEB staff to its response to G-Staff-3, pp.7-9.

In the response to G-Staff-3, pp.7-9, OEB staff does not note any discussion of the number years that Alectra Utilities would request for disposition of the balances under the 1575/1576 method. Please provide a direct response to the following questions:

a) For each of Figures 1 to 5 (capitalization policy impacts for all rate zones using the 1575/1576 approach, assuming disposition upon rebasing)[1] provided in G-Staff-7, please confirm that the input cell for "# of years of rate rider disposition period" preferred by Alectra Utilities is 1. If this is not confirmed, please indicate the number of the years of the rate rider disposition period that Alectra Utilities would request with supporting rationale.

b) For each of Figures 6 to 7 (capitalization policy impacts for using the 1575/1576 approach for BRZ and ERZ, assuming disposition in this proceeding for the 2017-2018 impacts) provided in G-Staff-7, please confirm that the input cell for "# of years of rate rider disposition period" preferred by Alectra Utilities is 1. If this is not confirmed, please indicate the number of the years of the rate rider disposition period that Alectra Utilities would request with supporting rationale.

Response:

a) Alectra Utilities does not agree with the impact of the capitalization policy change as presented by OEB Staff in Figures 1 to 5 of G-Staff-7. Please refer to Alectra Utilities' calculation of the impact of the capitalization policy change as identified in response to capitalization policy interrogatory G-Staff-3, filed October 7, 2019 and the further response provided to G-Staff-6 as part of this submission.

[1] OEB staff notes that the amounts for HRZ from 2017-2019 in Figure 1 and the amounts for PRZ in Figure 4 are for illustrative purposes at this time and would be adjusted for, or omitted, for the purposes of disposition.

Alectra Utilities recommends a one year disposition period, at the end of rebasing deferral period. The forecasted balances in the accounts is expected to range from $1.8MM to $17MM by the end of the rebasing deferral period. In Alectra Utilities' 2018 EDR Application, the Group 1 balances approved for disposition over a one-year period ranged from $7MM to $22MM. Therefore, a one-year disposition period is reasonable for the balances in the capitalization policy-related deferral accounts.

b) If the OEB directs disposition of the 2017 and 2018 balances as identified in G-Staff-3, in this rate proceeding, Alectra Utilities also recommends a one-year disposition period.

G-Staff-9

Reference: IRR G-Staff-4

Preamble:

In response to G-Staff-4 c), Alectra Utilities stated the following with respect to differentiating its proposed calculation methodology for the capitalization policy impacts from the methodology that the OEB applied to its legacy utilities under Account 1575/1576 in prior applications:

> **For Alectra Utilities' predecessors, Enersource, PowerStream, Horizon Utilities and Guelph, the Property, Plant and Equipment ("PP&E") values after the accounting policy change were higher than under previous CGAAP. Therefore, the return on rate base associated with the PP&E balance reflected a refund to customers to ensure that utilities did not collect the same amount of expenditures from customers twice. With respect to the impact of the capitalization policy change, the capital is not currently included in rate base and Alectra Utilities is not earning a return on this capital. Therefore, Alectra Utilities has calculated the return associated with this capital over the rebasing deferral period, which reflects an amount to be recovered from customers.**

OEB staff is seeking additional clarity on the distinction that Alectra Utilities has made between its proposed capitalization policy impact methodology and the OEB-approved 1575/1576 disposition methodology that its legacy utilities applied in previous years.

a) **Please confirm that the capitalized PP&E previously accounted for under the 1575/1576 method by the legacy utilities was also not included in their respective rate bases and those entities were not earning a return on that capital.**

   If this is not confirmed, please explain in detail.

b) **Please confirm that the PP&E values for Alectra Utilities after the capitalization policy change were higher than under previous capitalization policies (with the exception of Brampton RZ). Therefore, the return on rate base associated with the PP&E balance should reflect a refund to customers to ensure that Alectra Utilities does not collect the same amount of expenditures from customers twice.**

   If this is not confirmed, please explain in detail.

Response:

a) For Alectra Utilities' predecessor companies, the transition to International Financial Reporting Standards ("IFRS") resulted in a decrease in the amount of costs capitalized and an increase in operating expenses as utilities ceased the capitalization of general overhead costs, including labour burdens, general administration, material handling, and fleet burdens, for regulatory and external reporting under IFRS.

b) Please see Alectra Utilities' response to G-Staff-6 and G-Staff-7.

HRZ-Staff-9

Reference: IRR HRZ-Staff-1 a)
Reference: IRR G-Staff-15 Table 1 – Total Net Synergies Actual and Forecast

Preamble:

In response to OEB staff's table of historical OM&A costs populated from the RRR (Recordkeeping and Reporting Requirements) filings submitted by the legacy utilities from 2012-2016, Alectra Utilities noted that a one-time adjustment was required in the table to account for merger-related costs of $4,798,000 incurred by the Powerstream RZ in 2015.

In response to G-Staff-15 from the M-factor stream of this application, Alectra Utilities provided a net synergies table, showing transaction costs of $24.8 million incurred from 2015-2017.

a) Please confirm that the Powerstream RZ is the only legacy utility that recorded any merger-related costs on its books for the period of 2012-2016.

b) Please explain whether or not the $24.8 million in transaction costs from 2015-2017 have been factored into the historical figures of OM&A and capital that Alectra Utilities relied upon for the purposes of allocations in the ESM and CIVA calculations.

c) Please confirm that Alectra Utilities had previously reviewed the 2014-2016 historical OM&A figures used for the purposes of OM&A allocation and determined that the Powerstream RZ adjustment in 2015 is the only normalizing entry required to account for material one-off costs or anomalies in a given year.

Response:

a) All of Alectra Utilities' predecessor utilities recorded merger-related costs in their financial statements, for the period 2012-2016, if merger-related transaction costs were incurred in that year. All merger-related transaction costs were included in the annual RRR reporting of 2.1.7 Trial Balance. For the purposes of the annual RRR reporting of 2.1.5.6 ROE, all legacy utilities excluded merger-related transaction costs to determine regulatory ROE, except for Alectra Utilities' predecessor, PowerStream, for the 2015 reporting year.

b) The $24.8MM in transaction costs from 2015-2017 represent merger-related operating costs for the period January 1, 2015 to January 31, 2017 which were excluded from the historical figures of OM&A that Alectra Utilities relied upon for the purposes of allocations.

c) As provided in response to HRZ-Staff-2 a), Alectra Utilities relied on OM&A information from the OEB's Annual Yearbook of Electricity Distributors and adjusted the OM&A for merger-related transaction costs. The OEB's Annual Yearbook relies on data provided in the annual RRR 2.1.7 Trial Balance submission, which includes total OM&A prior to any required adjustments for the purposes of calculating the regulatory ROE. Alectra Utilities adjusted the Yearbook OM&A for each of the legacy utilities' amount of merger related transaction costs.

OEB Staff relied on OM&A figures from Alectra Utilities' predecessors' RRR 2.1.5.6 ROE annual filing which adjusts for all non-distribution related items, which includes merger-related transaction costs. For the reporting year 2015, Alectra Utilities' predecessor PowerStream was the only legacy utility that included merger transaction costs in the RRR 2.1.5.6 ROE annual filing; as a result, an adjustment was required to reduce OM&A to exclude merger-related transaction costs of $4,798,000.

HRZ-Staff-10

Reference: IRR HRZ-Staff-1
Reference: Attachment 11-Table of Allocations Horizon ESM 2018
Reference: Attachment 9-Table of Allocations Horizon ESM 2017

Preamble:

In HRZ-Staff-1, OEB staff prepared a historical OM&A table to show what the OM&A trends for each rate zone and Alectra Utilities as a whole are from 2012-2018.

Alectra Utilities stated the following with respect to explaining the primary drivers of the large reported increase in OM&A costs from 2016 to 2017:

> **The increase in OM&A costs from 2016 to 2017 was primarily driven by:**
>
> - **Increased costs to transition to monthly billing as mandated by the OEB;**
> - **One-time provision costs in 2017;**
> - **As a much larger organization than any of the individual legacy utilities, Alectra Utilities increased the resources dedicated to certain functions such as Internal Audit and the Project Management Office;**
> - **Normal inflationary increases for labour and materials; and**
> - **Wage harmonization for management staff.**

a) **Please provide the total costs charged to OM&A for each one of the bullet points listed above.**

b) **Please explain what the one-time provision costs in 2017 pertain to and what led to the recording of this provision.**

c) **Please explain whether or not the one-time provision costs in 2017 would have been recognized had the Alectra Utilities merger not taken place.**

d) **Please confirm that the increase in resources for functions such as internal audit and the project management office, as well as the wage harmonization for management staff, are permanent cost increases, as opposed to one-time costs incurred for 2017. If not, please explain.**

e) **Please provide additional information on what the wage harmonization for management staff costs entail. Specifically, whose wages are being harmonized and for what purposes.**

f) **Please provide detailed rationale for why Alectra Utilities has excluded each of the following items from the merger costs/savings in the Horizon ESM calculations for**

2017 and 2018 and why Alectra Utilities has deemed these items not to be merger-related:

- **i. One-time provision costs in 2017.**
- **ii. Increases in resources dedicated to certain functions such as Internal Audit and the Project Management Office to accommodate a much larger organization than any of the individual legacy utilities.**
- **iii. Wage harmonization for management staff.**

g) If Alectra Utilities has excluded the costs in part f) above in error, please revise the merger-related costs in the 2017 and 2018 ESM calculations and refile Attachments 9 and 11, as well as the updated supporting ESM models accordingly.

Response:

a) As provided in response to HRZ-Staff-1 c), each of Alectra Utilities predecessor utilities operated separate ERP systems with different charts of accounts and different ways of charging costs. Therefore, there is no common account structure or cost alignment in place to allow 2017 and 2016 OM&A to be compared at a detailed level. Alectra can provide costs increases related to monthly billing, $4.3 million, and the one-time provision costs, $3.6 million.

b) These are legal and environmental provisions specific to the ERZ and PRZ that do not impact the HRZ. These adjustments effectively reduce the total amount of OM&A allocated for the purpose of the ESM calculation, resulting in an increase to the ESM amount.

c) The provisions are not merger related and would have been recognized absent the merger.

d) The increases in resources for Internal Audit, the Project Management Office and the wage harmonization were permanent cost increases.

e) Each of the legacy utilities had their own unique organizational structures, positions and pay structures. After Alectra Utilities was formed the Company developed a new organizational structure, positions and a management pay structure. An open hiring process was established to populate all management positions. Employees had the opportunity to apply for management positions throughout the organization. As a result of differences in legacy pay structures some wage harmonization was required for management employees to ensure they were not being paid less than their staff and to ensure that there was a degree of wage fairness across comparable positions.

f) Responses to each section are as follows:

i. Details related to the one-time provision costs in 2017 were provided in the responses to part b and c above. The one-time provision costs in 2017 are not merger-related.
ii. The increases in resources dedicated to Internal Audit and the Project Management Office were merger-related costs and do not represent an OM&A cost driver for the increase in 2017.
iii. Wage harmonization for management staff was a merger-related cost and does not represent an OM&A cost driver for the increase in 2017.

g) The merger-related costs and savings have been tracked and recorded accurately for 2017 and 2018. The HRZ ESM has been accurately calculated for 2017 and 2018.

HRZ-Staff-11

Reference: IRR HRZ-Staff-1

Preamble:

In order to explain why the Horizon RZ's OM&A costs increased in 2018 from 2017, while every other RZ's OM&A costs decreased in 2018 from 2017, Alectra Utilities provided the following explanation:

> **There are three reasons which contribute to the Horizon Utilities RZ's OM&A costs increasing in 2018 from 2017 while every other rate zone's OM&A costs decreased in 2018 from 2017. First, the ESM results for 2017 (Attachment 9) includes actuals for one month (ERZ, HRZ, & PRZ) and two months (BRZ) where actual OM&A for HRZ was lower than the other rate zones. Secondly, in the 2017 allocation portion of OM&A, there were specific one time OM&A adjustments directly allocated to the ERZ and PRZ which effectively lowered the allocation of OM&A to HRZ. Finally, the capitalization policy change impact for the HRZ in 2018 was lower, which lowered the percentage OM&A allocation to HRZ in 2018.**

a) **Please provide the total OM&A costs for the one month of 2017 for ERZ, HRZ, and PRZ and the two months of 2017 for BRZ for the period before the legacy entities merged.**

Response:

a) Total OM&A costs, excluding merger-related transaction costs of $3MM, for the one month of 2017 for ERZ, HRZ, and PRZ and the two months of 2017 for BRZ for the period before the legacy entities merged is provided in Table 1, below.

Table 1 – Pre-merger OM&A

Rate Zone	Pre-merger OM&A
PowerStream RZ	$9,581,250
Enersource RZ	$5,168,238
Brampton RZ	$6,398,891
Horizon Utilities RZ	$5,266,751

These OM&A costs reconcile to the actual OM&A costs provided in Attachment 9 of EB-2019-0018 with the inclusion of the one-time provisions for the PowerStream and Enersource rate zones.

HRZ-Staff-12

Reference: IRR HRZ-Staff-1 a) "Table 1 – OM&A Allocations Horizon Utilities RZ ESM"

a) Please prepare a table similar to the one Alectra Utilities prepared in response to HRZ-Staff-1 a), showing what the total rate base for regulatory earnings was under each rate zone from 2012 to 2018. Please ensure that the 2017-2018 capitalization policy adjustments are shown separately for the purposes of adjusting opening and closing rate bases, as well as adjusting working capital allowances. If necessary, please explain any deviations made from the RRR filings submitted from 2012-2016.

b) As a result of the information presented in part a) of this question, if there are any significant variances in 2017 or 2018 rate bases (either by rate zone or Alectra Utilities as a whole) that are inconsistent from prior year trends, please provide an explanation and dollar amount of the key drivers for these variances.

Response:

a) Please see Table 1 below which shows the total rate base for regulatory earnings for each rate zone from 2012 to 2018 inclusive of the 2017 and 2018 capitalization policy adjustments. The 2012 – 2016 legacy utility reported rate base aligns with the annual RRR filings for each respective year.

Table 1 – 2012-2018 Rate Base ($MM)

	Rate Base					Change	
Year	HRZ	BRZ	ERZ	PRZ	Alectra	$	%
2012	412.1	341.8	575.0	795.6	**2,124.5**		
2013	451.4	367.2	629.4	836.3	**2,284.3**	159.8	7.5%
2014	472.7	388.3	645.2	893.0	**2,399.2**	115.0	5.0%
2015	477.3	402.0	706.2	980.5	**2,566.1**	166.9	7.0%
2016	506.5	421.7	777.7	1,064.9	**2,770.8**	204.7	8.0%
2017 - Adjusted	515.6	422.0	791.1	1,038.1	**2,766.7**	-4.1	-0.1%
2018 - Adjusted	530.1	434.6	827.8	1,090.4	**2,882.9**	116.1	4.2%
2017	517.6	421.3	791.7	1,038.1	2,768.8		
2017 Rate Base Adj	(2.0)	0.7	(0.7)	(0.1)	(2.1)		
2017 - Adjusted	**515.6**	**422.0**	**791.1**	**1,038.1**	**2,766.7**		
2018	537.3	432.2	830.2	1,090.8	2,890.5		
2018 Rate Base Adj	(7.2)	2.4	(2.4)	(0.4)	(7.6)		
2018 - Adjusted	**530.1**	**434.6**	**827.8**	**1,090.4**	**2,882.9**		

Tables 2 and 3 provide a reconciliation of capitalization policy related adjustments for 2017 and 2018.

Table 2 – 2017 Capitalization Policy Adjustments ($MM)

2017 Adjustments to Rate Base for Capitalization Policy Change	HRZ	BRZ	ERZ	PRZ	Alectra
2017 Adjustments to Average Net Fixed Assets:					
Remove capitalized OM&A	(5.40)	1.83	(1.87)	(0.19)	(5.63)
Add depreciation difference[1]	0.07	(0.02)	0.02	0.002	0.1
Total Adjustment to Closing Net Fixed Assets	(5.33)	1.81	(1.84)	(0.19)	(5.56)
Change in Average Net Fixed Assets[2]	(2.67)	0.90	(0.92)	(0.10)	(2.78)
2017 Adjustments to Working Capital Allowance:					
Adjustments to Working Capital Base controllable expenses:					
Add capitalized OM&A	5.40	(1.83)	1.87	0.19	5.63
Working Capital Rate	12.0%	13.0%	13.5%	7.5%	
Adjustment to Working Capital Allowance	0.65	(0.24)	0.25	0.01	0.68
Effects of Accounting Changes on Rate Base	**(2.02)**	**0.67**	**(0.67)**	**(0.08)**	**(2.10)**

1. Assumes 40 year assets and half year rule
2. First year of policy change (NFA opening = 0)

Table 3 – 2018 Capitalization Policy Adjustments ($MM)

2018 Adjustments to Rate Base for Capitalization Policy Change	HRZ	BRZ	ERZ	PRZ	Alectra
2018 Adjustments to Average Net Fixed Assets:					
Remove capitalized OM&A	(5.24)	1.61	(1.71)	(0.41)	(5.75)
Add depreciation difference[1]	0.20	(0.07)	0.07	0.010	0.2
2018 Total Adjustment to Closing Net Fixed Assets	(5.04)	1.54	(1.64)	(0.40)	(5.54)
2018 Closing NFA	(10.37)	3.35	(3.49)	(0.59)	(11.10)
Change in Average Net Fixed Assets	(7.85)	2.58	(2.66)	(0.39)	(8.33)
2018 Adjustments to Working Capital Allowance:					
Adjustments to Working Capital Base controllable expenses:					
Add capitalized OM&A	5.24	(1.61)	1.71	0.41	5.75
Working Capital Rate	12.0%	13.0%	13.5%	7.5%	
Adjustment to Working Capital Allowance	0.63	(0.21)	0.23	0.03	0.68
Effects of Accounting Changes on Rate Base	**(7.22)**	**2.37**	**(2.43)**	**(0.36)**	**(7.65)**

1. Assumes 40 year assets and half year rule

b) The average rate base increase from 2012-2016 is 6.9% for all rate zones. The change in rate base from 2016 to 2017 was a decrease of 0.1%; the change in rate base from 2017 to 2018 was an increase of 4.2%. The major driver of the decrease in the average rate base in 2017 and 2018 was the implementation of the Ontario Fair Hydro Plan. The Ontario Fair Hydro Plan was phased-in beginning in January 2017 with an 8% rebate and fully implemented on July 1, 2017 which resulted in eligible low volume consumers receiving a 25% average bill reduction. This implementation led to a significant reduction in cost of power and resulting working capital in 2017 and 2018. A variance analysis from 2016 to 2017 and 2017 to 2018 highlights the impact on working capital and decrease in average rate base over these years.

Table 4 – Rate Base Variance Analysis ($MM)

2016 vs 2017 Variance	**2016 Rate Base**					**2017 Rate Base**					**2017 vs. 2016 Rate Base $ Variance**					
	HRZ	**BRZ**	**ERZ**	**PRZ**	**Alectra**	**HRZ**	**BRZ**	**ERZ**	**PRZ**	**Alectra**	**HRZ**	**BRZ**	**ERZ**	**PRZ**	**Alectra**	**Alectra %**
Cost of Power	610.9	519.7	897.3	1,127.4	3,155.2	510.2	468.7	791.3	1,006.7	2,776.8	(100.7)	-51.0	(106.0)	(120.7)	(378.4)	-12.0%
OM&A	59.3	30.0	60.4	86.6	236.4	61.0	35.1	61.9	99.9	257.9	1.7	5.1	1.5	13.2	21.5	9.1%
Total Cost of Power & OM&A	**670.2**	**549.7**	**957.7**	**1,214.0**	**3,391.6**	**571.2**	**503.8**	**853.2**	**1,106.5**	**3,034.7**	**(99.0)**	**(45.9)**	**(104.5)**	**(107.5)**	**(356.9)**	-2.9%
Working Capital Allowance %	12.0%	13.0%	13.5%	13.0%		12.0%	13.0%	13.5%	7.5%							
Total Working Capital Allowance	**80.4**	**71.5**	**129.3**	**157.8**	**439.0**	**68.5**	**65.5**	**115.2**	**83.0**	**332.2**	**(11.9)**	**-6.0**	**(14.1)**	**(74.8)**	**(106.8)**	-24.3%
PPE																
Average regulated PP&E	**426.0**	**350.3**	**648.4**	**907.1**	**2,331.9**	**449.1**	**355.8**	**676.6**	**955.2**	**2,436.6**	**23.0**	**5.5**	**28.2**	**48.0**	**104.8**	4.5%
Capitalization Policy Change	N/A	N/A	N/A	N/A	N/A	(2.0)	0.7	(0.7)	(0.1)	(2.1)	(2.0)	0.7	(0.7)	(0.1)	(2.1)	0.0%
Total Rate Base	**506.5**	**421.7**	**777.7**	**1,064.9**	**2,770.8**	**515.6**	**422.0**	**791.1**	**1,038.1**	**2,766.7**	**9.1**	**0.2**	**13.4**	**(26.9)**	**(4.1)**	**-0.1%**

2017 vs 2018 Variance	**2017 Rate Base**					**2018 Rate Base**					**2017 vs. 2016 Rate Base $ Variance**					
	HRZ	**BRZ**	**ERZ**	**PRZ**	**Alectra**	**HRZ**	**BRZ**	**ERZ**	**PRZ**	**Alectra**	**HRZ**	**BRZ**	**ERZ**	**PRZ**	**Alectra**	**Alectra %**
Cost of Power	510.2	468.7	791.3	1,006.7	2,776.8	494.9	443.3	755.9	920.9	2,615.0	(15.3)	-25.4	(35.4)	(85.8)	(161.8)	-5.8%
OM&A	61.0	35.1	61.9	99.9	257.9	62.8	34.2	61.6	97.4	256.1	1.9	-1.0	(0.3)	(2.4)	(1.8)	-0.7%
Total Cost of Power & OM&A	**571.2**	**503.8**	**853.2**	**1,106.5**	**3,034.7**	**557.7**	**477.5**	**817.5**	**1,018.3**	**2,871.0**	**(13.4)**	**-26.4**	**(35.6)**	**(88.2)**	**(163.6)**	-6.5%
Working Capital Allowance %	12.0%	13.0%	13.5%	7.5%		12.0%	13.0%	13.5%	7.5%							
Total Working Capital Allowance	**68.5**	**65.5**	**115.2**	**83.0**	**332.2**	**66.9**	**62.1**	**110.4**	**76.4**	**315.7**	**(1.6)**	**-3.4**	**(4.8)**	**(6.6)**	**(16.5)**	-5.0%
PPE																
Average regulated PP&E	**449.1**	**355.8**	**676.6**	**955.2**	**2,436.6**	**470.4**	**370.1**	**719.9**	**1,014.4**	**2,574.8**	**21.3**	**14.3**	**43.3**	**59.2**	**138.1**	5.7%
Capitalization Policy Change	(2.0)	0.7	(0.7)	(0.1)	(2.1)	(7.2)	2.4	(2.4)	(0.4)	(7.6)	(5.2)	1.7	(1.8)	(0.3)	(5.5)	0.0%
Total Rate Base	**515.6**	**422.0**	**791.1**	**1,038.1**	**2,766.7**	**530.1**	**434.6**	**827.8**	**1,090.4**	**2,882.9**	**14.5**	**12.6**	**36.7**	**52.4**	**116.1**	**4.2%**

HRZ-Staff-12

ATTACHMENT 1 – Rate Base

HRZ-Staff-12 a.
Table 1 – 2012-2018 Rate Base ($MM)

Year	Rate Base					Change	
	HRZ	BRZ	ERZ	PRZ	Alectra	$	%
2012	412.1	341.8	575.0	795.6	**2,124.5**		
2013	451.4	367.2	629.4	836.3	**2,284.3**	159.8	7.5%
2014	472.7	388.3	645.2	893.0	**2,399.2**	115.0	5.0%
2015	477.3	402.0	706.2	980.5	**2,566.1**	166.9	7.0%
2016	506.5	421.7	777.7	1,064.9	**2,770.8**	204.7	8.0%
2017 - Adjusted	515.6	422.0	791.1	1,038.1	**2,766.7**	-4.1	-0.1%
2018 - Adjusted	530.1	434.6	827.8	1,090.4	**2,882.9**	116.1	4.2%
2017	517.6	421.3	791.7	1,038.1	2,768.8		
2017 Rate Base Adj	(2.0)	0.7	(0.7)	(0.1)	(2.1)		
2017 - Adjusted	**515.6**	**422.0**	**791.1**	**1,038.1**	**2,766.7**		
2018	537.3	432.2	830.2	1,090.8	2,890.5		
2018 Rate Base Adj	(7.2)	2.4	(2.4)	(0.4)	(7.6)		
2018 - Adjusted	**530.1**	**434.6**	**827.8**	**1,090.4**	**2,882.9**		

Capitalization Policy Adjustments

2017 Adjustments to Rate Base for Capitalization Policy Change	**HRZ**	**BRZ**	**ERZ**	**PRZ**	**Alectra**
2017 Adjustments to Average Net Fixed Assets:					
Remove capitalized OM&A	(5.40)	1.83	(1.87)	(0.19)	(5.63)
Add depreciation difference[1]	0.07	(0.02)	0.02	0.002	0.1
Total Adjustment to Closing Net Fixed Assets	(5.33)	1.81	(1.84)	(0.19)	(5.56)
Change in Average Net Fixed Assets[2]	(2.67)	0.90	(0.92)	(0.10)	(2.78)
2017 Adjustments to Working Capital Allowance:					
Adjustments to Working Capital Base controllable expenses:					
Add capitalized OM&A	5.40	(1.83)	1.87	0.19	5.63
Working Capital Rate	12.0%	13.0%	13.5%	7.5%	
Adjustment to Working Capital Allowance	0.65	(0.24)	0.25	0.01	0.68
Effects of Accounting Changes on Rate Base	**(2.02)**	**0.67**	**(0.67)**	**(0.08)**	**(2.10)**

1. Assumes 40 year assets and half year rule
2. First year of policy change (NFA opening = 0)

2018 Adjustments to Rate Base for Capitalization Policy Change	**HRZ**	**BRZ**	**ERZ**	**PRZ**	**Alectra**
2018 Adjustments to Average Net Fixed Assets:					
Remove capitalized OM&A	(5.24)	1.61	(1.71)	(0.41)	(5.75)
Add depreciation difference[1]	0.20	(0.07)	0.07	0.010	0.2
2018 Total Adjustment to Closing Net Fixed Assets	(5.04)	1.54	(1.64)	(0.40)	(5.54)
2018 Closing NFA	(10.37)	3.35	(3.49)	(0.59)	(11.10)
Change in Average Net Fixed Assets	(7.85)	2.58	(2.66)	(0.39)	(8.33)
2018 Adjustments to Working Capital Allowance:					
Adjustments to Working Capital Base controllable expenses:					
Add capitalized OM&A	5.24	(1.61)	1.71	0.41	5.75
Working Capital Rate	12.0%	13.0%	13.5%	7.5%	
Adjustment to Working Capital Allowance	0.63	(0.21)	0.23	0.03	0.68
Effects of Accounting Changes on Rate Base	**(7.22)**	**2.37**	**(2.43)**	**(0.36)**	**(7.65)**

1. Assumes 40 year assets and half year rule

HRZ-Staff-12 b.
Table 2 – Rate Base Variance Analysis ($millions)

2016 vs 2017 Variance	2016 Rate Base					2017 Rate Base					2017 vs. 2016 Rate Base $ Variance					
	HRZ	BRZ	ERZ	PRZ	Alectra	HRZ	BRZ	ERZ	PRZ	Alectra	HRZ	BRZ	ERZ	PRZ	Alectra	Alectra %
Cost of Power	610.9	519.7	897.3	1,127.4	3,155.2	510.2	468.7	791.3	1,006.7	2,776.8	(100.7)	-51.0	(106.0)	(120.7)	(378.4)	-12.0%
OM&A	59.3	30.0	60.4	86.6	236.4	61.0	35.1	61.9	99.9	257.9	1.7	5.1	1.5	13.2	21.5	9.1%
Total Cost of Power & OM&A	**670.2**	**549.7**	**957.7**	**1,214.0**	**3,391.6**	**571.2**	**503.8**	**853.2**	**1,106.5**	**3,034.7**	**(99.0)**	**(45.9)**	**(104.5)**	**(107.5)**	**(356.9)**	-2.9%
Working Capital Allowance %	12.0%	13.0%	13.5%	13.0%		12.0%	13.0%	13.5%	7.5%							
Total Working Capital Allowance	**80.4**	**71.5**	**129.3**	**157.8**	**439.0**	**68.5**	**65.5**	**115.2**	**83.0**	**332.2**	**(11.9)**	**-6.0**	**(14.1)**	**(74.8)**	**(106.8)**	-24.3%
PPE																
Average regulated PP&E	**426.0**	**350.3**	**648.4**	**907.1**	**2,331.9**	**449.1**	**355.8**	**676.6**	**955.2**	**2,436.6**	**23.0**	**5.5**	**28.2**	**48.0**	**104.8**	4.5%
Capitalization Policy Change	N/A	N/A	N/A	N/A	N/A	(2.0)	0.7	(0.7)	(0.1)	(2.1)	(2.0)	0.7	(0.7)	(0.1)	(2.1)	0.0%
Total Rate Base	**506.5**	**421.7**	**777.7**	**1,064.9**	**2,770.8**	**515.6**	**422.0**	**791.1**	**1,038.1**	**2,766.7**	**9.1**	**0.2**	**13.4**	**(26.9)**	**(4.1)**	**-0.1%**

2017 vs 2018 Variance	2017 Rate Base					2018 Rate Base					2017 vs. 2016 Rate Base $ Variance					
	HRZ	BRZ	ERZ	PRZ	Alectra	HRZ	BRZ	ERZ	PRZ	Alectra	HRZ	BRZ	ERZ	PRZ	Alectra	Alectra %
Cost of Power	510.2	468.7	791.3	1,006.7	2,776.8	494.9	443.3	755.9	920.9	2,615.0	(15.3)	-25.4	(35.4)	(85.8)	(161.8)	-5.8%
OM&A	61.0	35.1	61.9	99.9	257.9	62.8	34.2	61.6	97.4	256.1	1.9	-1.0	(0.3)	(2.4)	(1.8)	-0.7%
Total Cost of Power & OM&A	**571.2**	**503.8**	**853.2**	**1,106.5**	**3,034.7**	**557.7**	**477.5**	**817.5**	**1,018.3**	**2,871.0**	**(13.4)**	**-26.4**	**(35.6)**	**(88.2)**	**(163.6)**	-6.5%
Working Capital Allowance %	12.0%	13.0%	13.5%	7.5%		12.0%	13.0%	13.5%	7.5%							
Total Working Capital Allowance	**68.5**	**65.5**	**115.2**	**83.0**	**332.2**	**66.9**	**62.1**	**110.4**	**76.4**	**315.7**	**(1.6)**	**-3.4**	**(4.8)**	**(6.6)**	**(16.5)**	-5.0%
PPE																
Average regulated PP&E	**449.1**	**355.8**	**676.6**	**955.2**	**2,436.6**	**470.4**	**370.1**	**719.9**	**1,014.4**	**2,574.8**	**21.3**	**14.3**	**43.3**	**59.2**	**138.1**	5.7%
Capitalization Policy Change	(2.0)	0.7	(0.7)	(0.1)	(2.1)	(7.2)	2.4	(2.4)	(0.4)	(7.6)	(5.2)	1.7	(1.8)	(0.3)	(5.5)	0.0%
Total Rate Base	**515.6**	**422.0**	**791.1**	**1,038.1**	**2,766.7**	**530.1**	**434.6**	**827.8**	**1,090.4**	**2,882.9**	**14.5**	**12.6**	**36.7**	**52.4**	**116.1**	**4.2%**

HRZ-Staff-13

Reference: IRR HRZ-Staff-7 Table 3 – Reconciliation of 2017 actual versus forecast merger-related net capital costs

a) Please explain, in detail, the purpose of "Adjust for merger capital costs in WIP" in the amount of $22.0 million.

b) Why has Alectra Utilities included merger-related costs in WIP as an adjustment to in-service capital additions for the purposes of 2017 ESM? Please explain.

c) Please explain why 2017 is the only year affected by this adjustment. For example, are there merger costs/savings in the closing 2017 WIP that need to be removed and then added back in 2018 if the associated assets are deemed to be placed in service in 2018? Similarly, has Alectra Utilities included any merger-related costs/savings in the 2018 ESM adjustments that are part of the 2018 closing WIP account that should be adjusted for?

Response:

a) The $22MM adjustment is required in order to determine the net energized merger-related capital transition costs or savings. To be consistent with the methodology of determining rate base and depreciation expense, the merger-related capital costs that were work-in-progress at the end of the year must be removed. Please refer to interrogatory response HRZ-Staff-20 in EB-2018-0016 which provides the details of the calculation of the depreciation expense merger adjustment of $583,174 for Alectra Utilities for 2017. The HRZ share of this merger related depreciation expense is based on the proportion of Alectra Utilities' 2016 ending general plant depreciation which is 22.1%; this results in an allocation of $128,881.

b) Please see response to part a), above.

c) Similar to 2017, the 2018 energized merger-related transition costs exclude work-in-progress at the end of 2018. As provided in the response to interrogatory HRZ-Staff-7 a reconciliation of net merger capital costs and savings was provided in Table 4. All merger-related capital costs are general plant and the amounts presented include energized assets. The total Alectra Utilities general plant capital additions in 2018 were $57.9MM. This amount represents all general plant assets placed in service and therefore excludes any work-in-progress amounts. No further work-in-progress adjustments are required.

HRZ-Staff-14

Reference: IRR HRZ-Staff-7 Table 1 - Reconciliation of 2017 actual versus forecast merger-related net operating costs
Reference: IRR HRZ-Staff-7 Table 3 – Reconciliation of 2017 actual versus forecast merger-related net capital costs

Preamble:

In both of the tables where Alectra Utilities reconciles the 2017 and 2018 actual versus forecast merger-related net operating costs, a note is made that states:

> **Net OM&A merger results do not include pre-close synergies and transition costs recognized prior to the Alectra merger on February 1, 2017.**

a) Please explain why pre-close synergies and transition costs recognized prior to the Alectra Merger are not included? For example, if there are costs incurred by the legacy utilities in January 2017, are these merger-related costs not adjusted for in the directly allocated OM&A for 2017? If not, please explain why and quantify these amounts.

Response:

a) For the purposes of calculating the HRZ ESM for the 2017 year, as detailed in the evidence provided and the HRZ ESM model submitted in response to interrogatory SEC-64, the January 2017 stub period was calculated based on HRZ standalone financial statements, where merger-related transition costs were excluded for the one-month period. In addition, as provided in the response to HRZ-Staff-11, all rate zones' 2017 OM&A stub-periods were adjusted to exclude merger-related transaction costs in determining the regulatory return on equity found in Attachment 9 of EB-2019-0018.

HRZ-Staff-15

Reference: IRR HRZ-Staff-7 Table 5 Merger-related capital costs/savings drivers
Reference: IRR G-Staff-15 Table 1 – Total Net Synergies Actual and Forecast – M-factor Stream

Preamble:

OEB staff is unable to reconcile the figures provided in response to G-Staff-15 (Table 1) with the figures in Table 5 provided in response to HRZ-Staff-7. For example, transition costs charged to operating in 2017 are reported to be $21.8 million in Table 1 of G-Staff-15, while they are reported to be $18.1 million in HRZ-Staff-7 Table 5.

a) Please reconcile and explain the differences between the two tables referenced above and update the ESM and CIVA calculations and tables, if necessary.

Response:

a) Table 1 below identifies the difference between the reported amounts in Table 1 of Alectra Utilities' response to interrogatory G-Staff-15, and Table 5 of interrogatory HRZ-Staff-7. The differences identified represent the "pre-close" synergies and transition costs covering the period of 2016 and January 2017. In response to interrogatory G-Staff-15, Table 1 included all synergies and transition costs, including those that were recognized prior to the merger date of February 1, 2017. In interrogatory HRZ-Staff-7, Table 5 included actual transition costs and synergies recognized in 2017, after the effective date of the merger on February 1, 2017.

Table 1 – Reconciliation of IRR G-Staff-15 Table 1 and IRR HRZ-Staff-7 Table 5 ($000s)

Reconciliation	G-Staff-15, Table 1	HRZ-Staff-7, Table 5	Difference
Operating Transition Costs	21,838	18,161	3,677
Operating Synergies	(29,169)	(24,243)	(4,926)
Net Operating Synergies	**(7,331)**	**(6,082)**	**(1,249)**
Capital Transition Costs	25,097	22,794	2,303
Capital Synergies	(21,812)	(17,891)	(3,921)
Net Capital Synergies	**3,285**	**4,903**	**(1,618)**
Total Net Synergies	**(4,046)**	**(1,179)**	**(2,867)**

For the purposes of the 2017 HRZ ESM and CIVA calculations, OM&A and capital were adjusted for the full year impact of merger-related costs and savings. The merger-related adjustments included the post-merger-related costs and savings, as identified in HRZ-Staff-7 Table 5, and January 2017 merger-related costs, as provided in response to HRZ-Staff-11. Alectra Utilities confirms that no update is required to the ESM or CIVA calculations.

HRZ-Staff-16

Reference: IRR HRZ-Staff-7 - Table 5 – Merger-related capital costs/savings drivers

Preamble:

OEB staff notes that there are two categories that are the primary drivers between the OPEX savings in 2017 and 2018 forecast in the business plan versus the reported actual results, namely the consolidation of contracts and services and the consolidation of systems. OEB staff is seeking additional clarity on how Alectra Utilities calculated the actual and forecast savings in those categories.

a) Please provide the supporting documentation for how Alectra Utilities derived the 2017 and 2018 actual and forecast amounts in those two particular rows, preparing a bottom-up itemization of those amounts.

b) Please provide a detailed explanation for any significant components that constitute the amounts requested in part a) of this question.

Response:

a) A business unit summary of the itemized consolidation of contracts and services and the consolidation of systems are provided in Table 1 and Table 2, respectively.

Table 1 – Summary of Itemized Consolidation of Contracts and Services ($MM)

	Actuals		Forecast (Bus. Case)		Variance	
	2017	**2018**	**2017**	**2018**	**2017**	**2018**
Consolidation of contracts and services	**14.9**	**20.1**	**5.5**	**10.2**	**9.3**	**9.9**
Finance & Treasury	9.1	10.9	0.5	0.7	8.6	10.1
Implementation of Monthly Billing	1.6	0.6	0.4	-	1.2	0.6
Locates Synergies	0.4	1.6	-	-	0.4	1.6
Operations Contracts	0.3	1.3	0.1	0.1	0.2	1.2
Supply Chain Contracts	0.5	1.0	0.4	1.3	0.1	(0.2)
Memberships	0.0	0.5	-	-	0.0	0.5
Training & Development	0.1	0.1	0.0	0.0	0.0	0.0
Recruitment Services	0.2	0.1	0.3	0.1	(0.1)	-
Other	2.7	3.9	3.0	3.9	(0.3)	0.0
Rugulatory Consulting	-	0.3	0.3	0.3	(0.3)	(0.0)
Unrealized Synergy Targets	-	-	0.7	3.8	(0.7)	(3.8)

Table 2 – Summary of Itemized Consolidation of Systems ($MM)

	Actuals		Forecast (Bus. Case)		Variance	
	2017	**2018**	**2017**	**2018**	**2017**	**2018**
Consolidation of systems	**2.2**	**4.5**	**(5.1)**	**(4.9)**	**7.2**	**9.4**
Rate Application Decisions	-	-	(5.0)	(5.0)	5.0	5.0
IT - Maintenance and Services Synergies	0.1	(0.2)	(1.1)	(1.0)	1.2	0.8
IT - Other Synergies	1.2	3.9	0.0	0.0	1.1	3.9
Other synergies	0.6	0.6	0.4	0.2	0.2	0.4
IT - Contractor and Consulting Synergies	0.3	0.2	0.6	0.8	(0.3)	(0.6)

b) A significant component and the primary driver of the variance between actual and plan for consolidation of contracts and services is related to financing synergies. Financing synergies were not included in the merger business plan and represent $8.1 million in 2017 and $8.5 million in 2018. For the purposes of the HRZ ESM calculation, financing synergies were excluded from the identified OM&A merger savings. These financing synergies principally arose from a planned $675MM bond issuance in 2017 that was executed in May of that year at market interest rates that were materially below an assumed interest rate in the Alectra merger business case. The proceeds of the bond issuance were used to: i) refinance an acquisition credit facility used to acquire Hydro One Brampton for proceeds of $607.5MM; and ii) refinance Infrastructure Ontario loans supporting a non-regulated portfolio of rooftop solar generation projects in the former PowerStream Inc. (approximately $70MM of outstanding IO loans). The HRZ ESM relies on a deemed interest calculation which excludes the identified financing synergies in 2017 and 2018, and therefore has no impact on the HRZ ESM results.

A significant component of the variance between actual and plan for consolidation of systems are the results of 2017 PowerStream Custom IR application decision. That Application (EB-2015-0003) was not approved as a Custom IR; only a single forward test year cost of service rebasing was approved by the OEB for 2017. The outcome of the decision resulted in a reconciling item between the merger business case and the PRZ forecast. The reporting of the impact of this amount was included in the synergy report. The result of the decision was a cost structure reduction in the PRZ. In addition, direct labour allocation to transition projects contributed incremental operating synergies of $1.2 million in 2017 and $3.4 million in 2018.

HRZ-Staff-17

Reference: IRR HRZ-Staff-8

With respect to merger synergies, OEB staff is of the understanding that, in order to calculate the actual merger costs/savings, Alectra Utilities compares its actual operating and capital expenditures in 2017 and 2018 to what it estimates it would have spent on operating and capital costs had the merger not taken place (the counter-factual scenario).

a) **Please elaborate on OEB staff's understanding by explaining how Alectra Utilities calculates its counter-factual figures. Are they derived from the business plan that was put forth at the time of the MAADs application? Are they revised at the end of the actual year for new information that Alectra Utilities did not have when they were put together? Please explain in step-by-step detail.**

b) **Please confirm that when Alectra Utilities states that it tracks the actual merger savings, these are invariably estimates as well, since in order to calculate the savings attributable to the merger, the actual costs post-merger must be compared to an estimated, or forecast level of expenditures that Alectra Utilities believes would have occurred absent the merger (ie. the counter-factual is an estimate, and thus, the actual merger savings must be an estimate as well). If Alectra Utilities disagrees with this view, please explain.**

c) **When Alectra Utilities prepares its estimated actual merger-related costs and savings, how does it differentiate between foregone operating/capital costs (synergies) and normal operating efficiencies that might have been achieved whether the merger took place? For example, for any staffing positions that were vacated and deemed redundant post-merger, did Alectra Utilities undertake any review or exercise to determine if those positions might have remained unfilled simply by virtue of the legacy utility operating more efficiently? Please explain.**

Response:

a) Alectra Utilities compares actual operating and capital expenditures in 2017 and 2018 against the merger business plan that was put forward at the time of the MAADs application. The merger business plan was derived from the approved financial plans of each of the legacy organizations.

The merger business plan is not revised annually, however, new information that Alectra Utilities did not have is discussed with synergy business units and considered when evaluating and reporting actual costs and synergies.

b) Alectra Utilities tracks both actual and estimated cost savings. Actual cost savings are tracked and compared against the approved financial plans for the legacy organizations. Estimated cost savings include cost avoidances that are based on planned expenditures from the merger business plan, derived from the financial plans of each of the legacy organizations.

c) Alectra Utilities merger synergies are derived from the benefits achieved through consolidation, which include: savings from labour redundancies; systems consolidations; contracts and services consolidation; volume discounts; fleet and equipment rationalization; elimination of costs due to converged IT systems; and elimination of duplicated programming costs due to regulatory compliance or changes in regulation. Alectra Utilities differentiates between synergies and normal operating efficiencies by evaluating them on the basis of whether they would have occurred without the merger.

HRZ-Staff-18

Reference: IRR HRZ-Staff-8
Reference: IRR HRZ-Staff-1

Preamble:

With respect to providing a detailed variance analysis between 2016 and 2017 OM&A costs, Alectra Utilities stated:

> **Alectra Utilities is unable to provide a more detailed reconciliation of the changes in OM&A from 2016 to 2017. Each of Alectra Utilities' predecessor utilities operated separate Enterprise Resource Planning ("ERP") systems with different charts of accounts and different ways of charging costs. For example, in some legacy utilities, software licensing costs were all charged centrally to Information Technology ("IT") while in others they were decentralized. As a result, there is no simple way to combine the financial results of the legacy utilities and provide meaningful variance analysis. The account structures and treatment of costs were completely different. After the creation of Alectra Utilities, the Finance team worked to create a common mapping structure and align costs in order to report financial results in 2017. However, the process of aligning costs and mapping the four legacy account structures into a common reporting structure took several months to complete in 2017. Since Alectra Utilities was a new entity and was not required to report prior year comparative results for financial reporting purposes, this mapping and cost alignment exercise was not undertaken for 2016 results. Therefore, there is no common account structure or cost alignment in place to allow 2017 and 2016 OM&A to be compared at a detailed level for Alectra Utilities.**

a) Please confirm that, in order to calculate the forecast (and subsequently, the reported actual) merger-related costs and savings, Alectra Utilities relied on the pre-2017 financial mapping for the legacy utilities to project the counter-factual or status quo financial scenario (ie. the costs that all the entities would have incurred individually, had the merger not taken place). If this is not confirmed, please explain on what basis Alectra Utilities estimated the status quo costs (both for the purposes of the MAADs application, and the reporting of actual savings).

b) How does Alectra Utilities overcome the incomparable basis of financial cost mapping for the purposes of tracking and recording its actual monthly merger savings and costs? Specifically, if the amounts of operating and capital costs recorded in 2017 and 2018 are incomparable to pre-2017 financial mapping structures (which are presumably the basis for the counter-factual scenario of the 2017 and 2018 costs absent a merger), what exercises does Alectra Utility have to undertake so that actual costs post-merger can be fairly compared to the hypothetical status quo?

Response:

a) Alectra Utilities tracks both actual and estimated cost savings. Actual cost savings are tracked and compared against the approved financial plans for the legacy organizations. Estimated cost savings include cost avoidances that are based on planned expenditures from the merger business plan, derived from the financial plans of each of the legacy organizations.

b) Prior to the merger, management from the predecessor utilities evaluated the departments that would be a part of Alectra Utilities. The headcount was reviewed, and a determination was made regarding the requirement for the consolidated organization. The difference between existing headcount and the future Alectra Utilities headcount was identified. Similarly, management evaluated non-payroll expenses, such as rating agency evaluations, consulting support, IT support for corporate systems such as the ERP system and identified the amount that was required for the new organization. On consolidation, Alectra Utilities has manually tracked and compares actual merger costs and savings through regular meetings with synergy business units and the support of Finance business partners. Further, the integrity of the synergy reporting is supported through audits by Internal Audit in order to validate and compare merger costs and savings. Please also see Alectra Utilities' response to HRZ-Staff-19 which includes the internal audit reports for 2017 and 2018.

HRZ-Staff-19

Reference: IRR HRZ-Staff-8

Preamble:

Alectra Utilities stated the following with respect to tracking its merger-related costs and savings:

> **Alectra Utilities' actual merger savings and costs are tracked and recorded on a monthly basis. This information is reviewed and audited annually by Alectra Utilities' internal audit department.**

a) Please provide a copy of the internal audit reports referred to in the statement above for the 2017 and 2018 fiscal years.

Response:

a) The following internal audit reports for the 2017 and 2018 fiscal years are provided as Attachments 1 to 4:

- Synergy Savings Review, dated November 2017
- Synergy Savings Review, dated February 2018
- Synergy Savings Review, dated August 2018
- Synergy Saving Review, dated February 2019

The November 2017 report covers the February to July 2017 period; the February 2018 report covers the August to December 2017 period; the August 2018 report covers the January to June 2018 period; and the February 2019 report covers the July to December 2018 period.

HRZ-Staff-19

ATTACHMENT 1 – Synergy Savings Review, dated November 2017

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Discover the possibilities

Synergy Savings Review

Internal Audit Department
November 2017

CONTENTS

EXECUTIVE SUMMARY

Other than those identified by the client, there were no further material errors noted. Internal Audit has identified some recommendations for improvements in the process.

As part of our 2017 internal audit plan, we have recently completed a review of the synergy savings processes. The audit approach was discussed with management, and testing completed for the month ending July 2017. KPMG is in the process of reviewing Internal Audit's work and will provide additional guidance on the audit work completed as well as perform a full review of year end results.

The purpose of the review was to determine whether synergy savings and transition costs were accurately reported and whether targets were achieved as at July 2017.

The scope of the review consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Gain an understanding of the process used by Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including review of any automated reports or spreadsheets used
- Validate operating and capital synergies achieved in the quarterly report
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the quarterly report represent all costs incurred relating to merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

The following issues were identified by the client prior to the commencement of the audit;

1. Labour burden rate; this was corrected in future monthly reporting
2. Tracking management labour changes for staff transfers between departments below Director level; this continues to be a work in progress

The review highlighted three other areas requiring further management attention:

1. Base salary reporting
2. Inconsistencies among the severance information provided
3. Review of financing synergies

In general, there are controls in place to manage the synergy savings and cost reporting process and many recommended courses of action have already been put into place or are in the process of being implemented. Internal Audit noted that every department involved was very helpful in obtaining source documentation and answering any questions in a timely manner.

1. Introduction

As a result of the merger between Enersource Inc., Horizon Utilities Inc. and PowerStream Inc., coupled with the acquisition of Hydro One Brampton Networks Inc., Alectra Utilities Inc. was formed. The main premise was to provide greater savings and allow the combined resources to take advantage of key strengths and maximize synergies. The synergies were quantified and presented in a business case that Internal Audit was asked to verify. The synergy savings audit uses the information from the merger date, February 1, 2017, to July 31, 2017 (the last report provided) and was conducted from September to November 2017.

2. Audit Objective

As part of our internal audit plan, we have recently completed a review of the synergy savings and transition cost recording process. The purpose of the review was to determine whether synergy savings and transition costs were accurately reported and whether targets were achieved as at July 31, 2017.

The audit plan was discussed with management, and testing completed for the month ending July 2017. Our approach consisted of the following steps:

- Interviews with management in identifying how the numbers were generated
- Review of the process involved
- Recalculation of material dollar amounts tested and viewing source information

3. Audit Scope

The scope of the review consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Gain an understanding of the process used by Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including review of any automated reports or spreadsheets used
- Validate operating and capital synergies achieved in the quarterly report
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the quarterly report represent all costs incurred relating to the merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

The financial results for the months February 1 through July 31, 2017 were reviewed.

4. Client Accomplishments

It should be noted that the IMO has validated the capital synergies and there were no observations noted. In addition, the IMO has validated all labour savings with the various business groups. The IMO, Finance and People Services teams worked well together to ensure that labour reconciled to the values reported within the General Ledger and that all information regarding vacancies were tracked and reported on a timely basis.

5. Issues Identified By Client

Labour Burden Rate

The overhead burden rate that was being applied to the labour synergies and costs was 54%. This was applied to the base salaries in order to determine the total impact of Voluntary Severance Packages and retirement packages. Management agreed that a revision of the burden rate was required from the one used previously in the business case.

IMO provided an updated July-August Labour Synergy report, reflecting a rate change to 31% for union staff and 29% for management staff, producing a decrease in labour synergies of approximately $865K. Management believes that there will be a corresponding decrease in transition costs as well.

Tracking Management Labour Changes for Staff Transfers between Departments below Director Level

As per discussion with the IMO team, it was noted that the changes and tracking of headcounts were done accurately at the Director level and above, as that is where most severance and VSP level tracking was required. However, below that level, transfers were not tracked as consistently. As a result, the financial impact of this issue cannot be assessed at this time.

The IMO team receives information from various sources and at times things can go undetected and unreported due to many moving parts. This information can be difficult to reconcile and the IMO team does their best to update the information whenever it is required. According to the team, they did not have enough time to track it, and it is highly possible that the savings have been understated.

Going forward, the IMO has stated that efforts are underway to track all staff movements below the Director level. They are putting in a process by year-end that will accurately track all movements for all levels in one central database. This staffing database will be done in Access and should be ready for the year-end review. Additional findings and adjustments will be reflected at this time.

6. Key Observations and Recommendations

Recommendations were developed through discussions with Finance and the Integration Management Office (IMO), along with results from detail testing.

Observation #1 Priority: High	**Base Salary Reporting**
	There are differences in base salaries reported between the IMO and Finance for VSP's and severance amounts. As per discussion with People Services and review of the total severance information provided by Finance and the IMO team, differences in the base salaries were noted. Internal Audit observed 13 instances that had different base salaries reported. As noted by People Services, there are different versions of the same information among various business units. There may have been different assumptions used in reporting the same information among the various groups. The total base salaries reported by Finance are $329K higher within their spreadsheet than those reported within the General Ledger and the IMO report. The Manager, People Services also noted from the sheet provided by Finance that there were people missing from the list who received a VSP or Severance. The Manager, People noted that Finance suggested there were some difficulties in reconciling the headcount information. *Risk: Inaccurate base salaries reported could lead to errors in synergy reporting and incorrect severance payments.*
Recommendation	We recommend that People Services, Finance, IMO and Payroll all coordinate and use the same information for their reporting and tracking purposes. This will help with version control and ensure everyone is utilizing current information. One centralized process and version should be used to ensure all information is consistent and accurate amounts are reported and paid. The Manager, People Services has confirmed that they will map out a new process once they have corrected any discrepancies on Finance's existing tracker.
Response from Management	For the month of October, People Services and Finance will validate salaries and all related severance commitments. In 2018, a new process will be mapped out to ensure a central reporting of severance packages to Finance with all functions relying on one central document. Any base salary provided by People Services must not be altered by any other function without prior discussion with People Services and clarity for the reason of change. Other functions may add additional items and comments, based on the People Services-provided compensation and severance conditions.

	Respecting the list of VSP and Severances, People Services acknowledge that some exiting staff was missing from the synergy reporting. This was originally intentional, since we had been advised that non-synergy exits would be the liability of the terminating function. That decision has been reversed such that all 2017 Not-for-Cause termination decisions are to be tracked and costed in the Synergy budget. We have rectified this in October.
	To be Actioned By: Boukette Pezzin, Manager, People Services
	Estimated implementation date:

Observation #2 Priority: Medium	**Inconsistencies among the severance information provided.** During our review of the Voluntary Severance Packages (VSP) and severance packages, we noted the following: • There were two instances where witness sign off for Alectra had not been completed • There were two instances where Alectra did not sign the People Services portion, even though the employee had signed • Witness portion completed and signed by same person for employee and Alectra, even though Alectra People Services portion was not signed • There were three instances where financial amounts were not listed at all in the severance agreements • Resignation date is different on severance document than on severance liability worksheet *Risk: VSP and severance information recorded may not be accurate. Not signing documents can open the company up to undue legal exposure.*
Recommendation	VSP and severance information should be reviewed to ensure completeness and accuracy in the information agreed upon. In addition, not having the appropriate sign-offs made explicit can expose the company to potential disputes regarding severance packages. Going forward, all information should be reconciled and all sign-offs should be completed.
Response from Management	• Management appreciates this observation and will ensure going forward that all witnesses are properly signed off. • For clarity, there is no "People Services portion" for sign off on Alectra severance documents. All such documents are signed by the terminee and the leader of the relevant terminating function. In both instances where Alectra leadership did not sign off the on the final termination document, multiple previous versions had been prepared and signed. The final document was not signed by oversight. Management accepts culpability for these oversites and will commence a new sign off process. This process is that the Employee shall sign and accept first (once all amendments have been concluded) and the terminating leader will sign in approval thereafter, and only once. • The terminee's witness made a simple error in signing the incorrect witness spot. They re-signed correctly. If we deploy the sign off procedure noted above, the signing manager would have seen and corrected the mistaken witness. This process will address this witnessing error in future. With respect to unlisted financial commitments in a severance document, the People Services team should be advised which specific files are referenced in order to provide a specific answer and remedy.

	In the absence of that clarity, we are assuming that the severance dollar value was not articulated due to an elongated working notice period. It is our belief that the letters indicate a severance payment duration based on the base salary at the time of execution. Please confirm and provide file specifics so that the People Team can more properly investigate. Conversely it may be that the 3 files noted in the above Observation #2, are early terminations that were executed in advance of the final process/standard documentation/cost formula. Again, if we are provided with specifics on the files, we will more accurately respond and correct going forward. The revised process discussed in response to Audit Observation #1 will ensure that the resignation dates are validated and aligned.
	To be Actioned By: Boukette Pezzin, Manager, People Services
	Estimated implementation date:

Observation #3 **Priority: Low**	**Review of financing synergies** After discussion with the Director of Treasury, it was noted that the interest costs are understated by $45-50K as a result of the change in recognizing the interest on the debt. When the interest on the $675M debt was first recorded, it was done using the methodology from one of the former utilities, which was to start booking and recognizing interest the day after the debt was issued. However, to be more consistent with current policies, this will be amended to reflect interest on the first day the debt was issued. This adjustment will be reflected in the October statements. *Risk: Costs are understated and financing synergy reporting is not accurate.*
Recommendation	Discussion with the Director of Treasury has indicated that this adjustment will be shown on the October statement, which will show an increase in transition costs in the May balance when the debt was issued.
Response from Management	The October IMO report has been updated to reflect the revised financing synergies forecast provided by the Director of Treasury in November, which forecasts full year synergies of $8,114,819 and October year-to-date achieved synergies of $6,922,805. The Director of Treasury has confirmed that actuals have not been updated to account for understated interest costs of $45-50K and that this adjustment will be reflected in the November IMO update. **To be Actioned By:** Barb Gray, VP, Integration Management Office **Estimated implementation date: November 2017 Reporting**

7. Additional Item for Consideration

It is important to note that Internal Audit reviewed actual values and did not review forecasted information prepared by IMO.

8. Follow-Up Procedures

In general, controls are in place to manage the synergy savings and transition cost process and many recommended courses of action have already been put into place or are in the process of being actioned. IMO has been working diligently to improve all facets of the reporting and has accomplished a lot given a short time frame, limited information at times and a variety of databases.

9. Overall Assessment

Other than those identified by the client, there were no further material errors noted. Internal Audit has identified some recommendations for improvements in the process.

10.Acknowledgement of Review

Name and Title	Signature	Date
Garen Boduryan, Manager, Integration Reporting	[illegible]	Nov 24, 2017
Boukette Pezzin Manager, People Services	[illegible]	Nov. 27, 2017
Barb Gray, VP, Integration Management Office	Barb Gray	Nov 24/17
Kathy Lerette SVP, Business Transformation	Kathy Lerette	Nov 30/17
Kimberly Boyle SVP, People and Safety	[illegible]	Nov 27/17

APPENDIX A: Labour Synergies vs. 2015 Business Case

Internal Audit reviewed the labour synergies reported vs. the 2015 Business Case. It was noted that IMO relies on the individual business units and the People Group to provide their input and validation for the reports they provide. The IMO is aware that improvements to the process are required and are currently undertaking steps to correct that. They will have a central database by the end of the year to eliminate most of the back end validation and instead have that happen upfront before any reports are run and numbers are generated. Internal Audit was able to sample and verify the vacancies used in the synergy reporting.

The July 2017 differences reported by the IMO vs. the 2015 Business Case are as follows:

OM&A Net Savings	$6,395,368
Capital Net Savings	$ 0
Total Net Savings	**$6,395,368**
Business Case	$4,185,302
Variance	**$2,210,066**
Vacant-Redundant Positions	93
Avoided Headcount Positions	21
Total Net Headcount Reductions	114
Business Case	66
Variance	**48**

93 positions were deemed vacant-redundant as at July 2017, in addition to 21 headcount reductions for PowerStream avoided headcount totalling 114 net headcount reductions. This is favourable to the 66 predicted in the Business Case, giving a positive variance of 48. Per the IMO team, this is the result of people deciding to leave earlier through VSPs or other reasons than noted in the Business Case. In addition, business units realized some positions did not require the backfill they expected.

Internal Audit was recently made aware of management's decision to rebase the 2015 Business Case to the 2017 Financial Plan, requiring all comparisons to the business case to now be performed against the 2017 Financial Plan. This change will be reflected in the reports going forward and the IMO team will be implementing these changes into an updated model that runs the reports. This update will likely be tested in the year-end audit after all the adjustments have been made and reflected.

APPENDIX B: Financial Impact

Issues and Observations	Impact
1. Labour Burden Rate	($864,617) Unfavourable
2. Tracking of Changes	Not available at this time.
3. Base Salary Reporting	Not available at this time.
4. Severance Contract Information	No impact.
5. Financing Synergies	($50,000) Unfavourable
Total Impact – Sum of Issues (A)	($914,617)
Original Variance Reported - Appendix A (B)	$2,210,066
Adjusted Variance after Impact (A + B)	$1,295,449

APPENDIX C: Risk Rating Key

The following findings rating system has been established for evaluating the urgency of recommendations to be addressed:

High Priority	Observations rated "*high priority*" is due to the existence of either a significant internal control weakness for the business unit or significant operational efficiency improvement opportunity.
Medium Priority	Observations rated "*medium priority*" is due to the existence of an internal control weakness with some mitigating controls or an opportunity for operational efficiency improvements.
Low Priority	Observations rated "*low priority*" are not critical for the business unit, but should be addressed to either improve internal controls or minor operational efficiency opportunities.

HRZ-Staff-19

ATTACHMENT 2 – Synergy Savings Review, dated February 2018

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Synergy Savings Review

Internal Audit Department
February 2018

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EXECUTIVE SUMMARY

After a review of the process and supporting information, no material errors were noted. Internal Audit has identified some recommendations for improvements in the process.

As part of our 2018 Internal Audit plan, we have recently completed a review of the 2017 synergy savings processes. The audit approach was discussed with management, and testing completed for the year ended December 31, 2017. Internal Audit and KPMG performed a review of operational synergy savings and transition costs for the months of February through July 2017 and had KPMG review the audit work completed in the prior audit. KPMG has been engaged to perform a review of Internal Audit's year end results as well.

The purpose of the review was to determine whether synergy savings and transition costs were accurately reported as at December 2017.

The scope of the review consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Gain an understanding of the process used by Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including review of any automated reports or spreadsheets used
- Validate operating and capital synergies and costs reported
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the monthly report represent all costs incurred relating to merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

The review highlighted areas requiring further management attention:

1. Labour tracking document
2. IMO team continuity
3. Minor reporting errors

In general, there are controls in place to manage the synergy savings and cost reporting process and many recommended courses of action have already been put into place or are in the process of being implemented.

Overall assessment: Effective with opportunity for improvement

1. Introduction

As a result of the merger between Enersource Inc., Horizon Utilities Inc. and PowerStream Inc., coupled with the acquisition of Hydro One Brampton Networks Inc., Alectra Utilities Inc. was formed. The main premise was to provide greater savings and allow the combined resources to take advantage of key strengths and maximize synergies. The synergies were quantified and presented in a business case that Internal Audit was asked to verify. This audit focused on information from the end of the last audit, the period August 1, 2017 to December 31, 2017.

2. Audit Objective

As part of our internal audit plan, we have recently completed a review of the synergy savings and transition cost recording process. The purpose of the review was to determine whether synergy savings and transition costs were accurately reported and whether targets were achieved as at December 31, 2017.

The audit plan was discussed with management, and testing completed for the year ending December 2017. Our approach consisted of the following steps:

- Interviews with management in identifying how the numbers were generated
- Review of the process involved
- Recalculation of material dollar amounts tested and viewing source information

3. Audit Scope

The scope of the review consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Gain an understanding of the process used by Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including review of any automated reports or spreadsheets used
- Validate operating and capital synergies achieved in the monthly report
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the monthly report represent all costs incurred relating to the merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

The financial results for the months August through December 2017 were reviewed.

4. Client Accomplishments

It should be noted that the IMO has validated the capital synergies and expenditures and there were no observations noted. In addition, the IMO has validated all labour savings with the various business groups. The IMO, Finance and People Services teams worked well together to ensure that labour reconciled to the values reported within the General Ledger and that all information regarding vacancies were tracked and reported on a timely basis. They have done a great job in streamlining their processes and as a result, reporting the monthly synergies and costs has greatly improved.

5. Key Observations and Recommendations

Recommendations were developed through discussions with the Integration Management Office (IMO) and People Services, along with results from detail testing.

Observation #1 Priority: Medium	**Labour Tracking Document**
	The IMO group started a database to extract HR labour data regarding labour changes and employee movements and map it to financial data regarding vacancies/redundancies as well as cost savings which the IMO and Finance could validate and report. The person responsible for creating and mapping the database retired unexpectedly in early January 2018. The transition to maintain the required tracking document has been passed onto People Services. At this time, ownership of the various components of the tracking document and defined roles and responsibilities have not been fully outlined.
Recommendation	We recommend that People Services and the IMO team work together to ensure clearly defined roles and responsibilities and processes be documented to ensure ownership of data and timely reporting as required.
Response from Management	People Services will work with IMO to review process, and establish a transition plan, timelines and process documentation to ensure the required reporting is provided.
	To be Actioned By: SVP, People & Safety, Kimberly Boyle SVP, Business Transformation, Kathy Lerette
	Estimated implementation date: End of Q1 2018

Observation #2 **Priority: Medium**	**IMO team continuity**
	The IMO team that helps to put together the synergy and cost information has recently undergone changes, resulting in significant reduction in team size and will continue to reduce in numbers. As of the end of January, they have lost a Director and the person responsible for creating the labour tracking sheet; which has since been passed on to the People Services team. In the coming months, they will also be losing another member that made contributions to the synergy and labour reporting packages. The lack of continuity could result in knowledge loss.
Recommendation	We recommend that the IMO team review the opportunity to extend transitional staff to help with the transfer of knowledge to the remaining team and ensure that processes and workload are managed.
Response from Management	The IMO is currently undergoing a planning review and is assessing staff resource needs, based on 2018 planned activities that include; refining data inputs, updating report and forecast tools, automating processes, enhancing business support, and sustaining existing reporting deliverables. The IMO recognizes that additional support may be required and is evaluating alternatives, including extending transitional staff, to ensure workloads are manageable and that deliverables can be met.
	To be Actioned By: VP, Integration Management Office, Barb Gray
	Estimated implementation date: End of Q1 2018

Observation #3 **Priority: Low**	**Minor Reporting Errors**
	As part of Internal Audit's review, we noted that the following items were incorrectly recorded: • The charge for accounting valuation and services was double counted in the amount of $66,739. The IMO agrees that it has been double counted and will be adjusted for in the next reporting period. • Moving costs related to John St. were transposed when recorded on the tracking spreadsheet, resulting in an immaterial difference.
Recommendation	We recommend that these amounts be adjusted in the next period and closer attention should be paid to ensure it does not happen on a larger scale.
Response from Management	The IMO has corrected the accounting valuation and services double counting error and moving costs error in the January 2018 IMO synergy report.
	To be Actioned By: Manager, Integration Reporting, Garen Boduryan
	Estimated implementation date: Completed

6. Additional Item for Consideration

It is important to note that Internal Audit reviewed actual values and did not review forecasted information prepared by IMO.

7. Follow-Up Procedures

In general, controls are in place to manage the synergy savings and transition cost process. The IMO has been working diligently to improve all facets of the reporting and has improved the process significantly since the last review.

8. Overall Assessment

Internal Audit has identified some recommendations for improvements in the process. This audit has been rated as ***'Effective with opportunity for improvement.'***

9. Acknowledgement of Review

Name and Title	Signature	Date
Garen Boduryan, Manager, Integration Reporting	[illegible]	Feb. 20/2018
Boukette Pezzin Manager, People Services	[illegible]	Feb. 20/18
Barb Gray, VP, Integration Management Office	Barb Gray	Feb 20/18
Kathy Lerette SVP, Business Transformation	Kathy Lerette	Feb 20/18
Kimberly Boyle SVP, People and Safety	KBoyle	Feb 20/18

APPENDIX A: Labour Synergies vs. Business Case

Internal Audit reviewed the labour synergies reported vs. the Business Case. It was noted that IMO relies on the individual business units and the People Services group to provide their input and validation for the reports they provide. Internal Audit was able to sample and verify the vacancies used in the synergy reporting.

The December 2017 differences reported by the IMO vs. the Business Case are as follows:

OM&A Net Savings	$10,710,860
Capital Net Savings	$ 0
Total Net Savings	**$10,710,860**
Business Case	$ 7,673,054
Variance	**$ 3,037,806**
Vacant-Redundant Positions	148
Avoided Headcount Positions	21
Total Net Headcount Reductions	169
Business Case	66
Variance	**103**

148 positions were deemed vacant-redundant as at December 2017, in addition to 21 avoided headcounts, totalling 169 net headcount reductions. This is favourable to the 66 predicted in the Business Case, giving a positive variance of 103. Per the IMO team, this is the result of people deciding to leave earlier through VSPs or other reasons than noted in the Business Case. In addition, business units realized some positions did not require the backfill they expected.

APPENDIX B: Risk Rating Key

The following findings rating system has been established for evaluating the urgency of recommendations to be addressed:

High Priority	Observations rated "*high priority*" is due to the existence of either a significant internal control weakness for the business unit or significant operational efficiency improvement opportunity.
Medium Priority	Observations rated "*medium priority*" is due to the existence of an internal control weakness with some mitigating controls or an opportunity for operational efficiency improvements.
Low Priority	Observations rated "*low priority*" are not critical for the business unit, but should be addressed to either improve internal controls or minor operational efficiency opportunities.

HRZ-Staff-19

ATTACHMENT 3 – Synergy Savings Review, dated August 2018

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Synergy Savings Review

Internal Audit Department
August 2018

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EXECUTIVE SUMMARY

As part of our 2018 Internal Audit Plan, we recently completed a review of the synergy savings and transition costs captured in 2018. The audit approach was discussed with management, and testing completed for the six month period January through June 2018.

The purpose of the review was to determine whether synergy savings and transition costs, incurred since December 2017, had been accurately reported as at June 30, 2018.

The scope of the audit consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Understand the process used by People Services, Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including a review of any automated reports or spreadsheets used
- Validate operating and capital synergies and costs reported
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the monthly reports represent all costs incurred relating to merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

After a review of the process and supporting information, no material errors were noted. Internal Audit has identified the following areas requiring further management attention:

1. Non-Synergy Related Severance
2. Process Documentation

In general, there are controls in place to manage the synergy savings and transition costs reporting process. Many recommended courses of action from prior audits have already been put into place or are in the process of being implemented.

Overall assessment: Effective, with opportunity for improvement

1. Introduction

As a result of the merger between Enersource Inc., Horizon Utilities Inc. and PowerStream Inc., coupled with the acquisition of Hydro One Brampton Networks Inc., Alectra Utilities Inc. was formed. The main premise was to provide greater savings and allow the combined resources to take advantage of key strengths and maximize synergies. The synergies were quantified and presented in a business case that Internal Audit was asked to verify. This audit focused on information submitted from the end of the last audit, covering the period January 1, 2018 to June 30, 2018.

2. Audit Objective

As part of our internal audit plan, we recently completed a review of the synergy savings and transition cost recording process. The purpose of the review was to determine whether synergy savings and transition costs were accurately reported for the six month period ending June 30, 2018.

The audit plan was discussed with management, and testing completed for the period covering January 1 through June 30, 2018. Our approach consisted of the following steps:

- Interviews with management in identifying how the numbers were generated
- Review of the process involved
- Review of source documents
- Recalculation of material dollar amounts

3. Audit Scope

The scope of the review consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Understand the process used by the People Services, Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including a review of any automated reports or spreadsheets used
- Validate operating and capital synergies achieved in the monthly report
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the monthly reports represent all costs incurred relating to the merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

The financial results for the months January through June 2018 were reviewed.

4. Client Accomplishments

The IMO, People Services and Finance have been working diligently to improve and streamline all facets of the reporting process and as a result, the reporting of monthly synergies and costs has greatly improved. The teams have implemented the recommendations from prior Internal Audit reviews and incorporated them into their processes. This included bringing back staff members to ensure that processes and procedures would continue to operate as desired and the transfer of information would be seamless. It should also be noted that the IMO has validated all labour savings with the affected business units.

5. Key Observations and Recommendations

Recommendations were developed through discussions with the Integration Management Office (IMO), Finance and People Services, along with results from detail testing.

Observation #1 Priority: Medium	**Non-Synergy Related Severance**
	During our review we noted that severance information reported on a spreadsheet, provided by Finance to the IMO, included names, amounts and information of individuals not required for the Synergy reporting process. People Services agreed that this information should not have been disclosed to the IMO, as it was not required for Synergy reporting. The draft procedural document outlines that only the aggregate dollar amounts of non-synergy related costs are to be provided to the IMO as opposed to specifics; this allows for reconciliation between synergy and non-synergy related costs.
Recommendation	Due to the highly sensitive and confidential nature of severance information, we recommend that People Services limit reporting of severance data to those individuals that are required to have this knowledge to capture and report on synergy related costs and savings. People Services agreed this was an oversight and will not be provided in the future as it is not related to the Synergy reporting process.
Response from Management	The severance reporting procedure will be modified such that the final severance report will be provided directly from the People Services team to the IMO. This will ensure that a People Services representative can review and exclude details pertaining to non-synergy severances or other confidential information from the severance reporting from Finance. The People Services team will include the total aggregate amount for non-synergy severances as reference only, without identifying names of individual signees.
	To be Actioned By: Manager, People Services
	Estimated implementation date: September 1st 2018

Observation #2 **Priority: Medium**	**Process Documentation**	
	During our review of Synergy Reporting, we noted that there was no procedural documentation in place for their processes. There have been recent changes to the group structure and staffing and current processes being undertaken. In addition, there is heavy reliance on select individuals to produce the reporting packages. This includes the synergy reporting process as well as the labour synergy reporting process. The person responsible for labour synergy reporting will be transitioning these responsibilities in the coming months. A lack of procedural documentation presents a risk that reporting may not be completed on a timely basis if select individuals are away for any particular amount of time.	
Recommendation	We recommend that processes and procedures be documented. This would mitigate the risk of reporting not being completed in the event that the person responsible is away for any period of time. As the synergy reports are of high priority and status, it is important to ensure that this process continue uninterrupted. With the creation of process and procedural documentation, the responsibility to prepare the required documentation can be transferred to another staff member, as required, in a timely and seamless manner.	
Response from Management	The IMO will develop procedural documentation for key IMO processes including: updating labour and non-labour synergy reports, updating the labour synergy forecast model, updating risks and opportunities, and updating key management reports including EC presentation.	
	To be Actioned By: Manager, Integration Reporting	
	Estimated implementation date: December 31st, 2018	

6. Additional Items for Management Consideration

The point below was identified as a service to management. It does not require a response and is provided to assist with building more effective and efficient processes.

During our review of the severance documents we noted that there were some minor errors in recording and tracking the amount of severance for one employee and the effective date of payment for another. In another instance, the company's name was spelled wrong in the severance document provided to one employee. Errors in severance documents could create an opportunity for legal disputes and controversy. It is recommended that a further review be done of severance agreements to ensure the accuracy of information. This is especially true of legal documents where the possibility exists for potential ramifications due to a small error or technicality.

7. Overall Assessment

It is important to note that Internal Audit reviewed actual values and did not review forecasted information prepared by IMO.

Internal Audit has identified some recommendations for improvements in the process. This audit has been rated as ***'Effective, with opportunity for improvement.'***

8. Acknowledgement of Review

Name and Title	Signature	Date
Garen Boduryan, Manager, Integration Reporting		10/ 01/18
Boukette Pezzin Manager, People Services		10/01/18
Barb Gray, SVP, People and Safety	Barb Gray	10/01/18

APPENDIX A: Synergies vs. Business Case

Internal Audit reviewed the synergies reported vs. the 2017 Business Case. It was noted that IMO relies on the individual business units and the People Services group to provide their input and validation for the reports they provide.

Labour Synergies

The June 2018 Labour Synergies reported by the IMO vs. the Business Case are as follows:

OM&A Net Savings	$ 9,078,584
Capital Labour Net Savings	$ 839,748
Total Net Savings	**$ 9,918,332**
Business Case	$ 8,176,524
Variance	**$ 1,741,808**
Vacant-Redundant Positions	137
Avoided Headcount Positions	21
Total Net Headcount Reductions	158
Business Case	128
Variance	**30**

137 positions were deemed vacant-redundant as at June 2018, in addition to 21 avoided headcounts, totalling 158 net headcount reductions. This is favourable to the 128 predicted in the Business Case, giving a positive variance of 30 headcount. Per the IMO team, this is the result of people deciding to leave earlier through VSPs or other reasons than noted in the Business Case.

Net Capital Synergies

The June 2018 Net Capital Synergies reported by the IMO vs. the Business Case are as follows:

Net Capital Synergies	**$ -108,552**
Business Case	$ -9,689,723
Variance	**$ 9,581,171**

Total capital synergies include prorated savings for the early recognition of HOBNI CIS replacement synergies, planned for in the 2019 budget ($14M). The decision to recognize these savings earlier was corroborated through the 2019 capital planning process, which validated the removal of this project from the plan.

Net Operating Synergies

The June 2018 Net Operating Synergies reported by the IMO vs. the Business Case are as follows:

Net Operating Synergies	**$ 13,579,287**
Business Case	$ 6,287,800
Variance	**$ 7,291,487**

APPENDIX B: Risk Rating Key

The following findings rating system has been established for evaluating the urgency of recommendations to be addressed:

High Priority	Observations rated "*high priority*" is due to the existence of either a significant internal control weakness for the business unit or significant operational efficiency improvement opportunity.
Medium Priority	Observations rated "*medium priority*" is due to the existence of an internal control weakness with some mitigating controls or an opportunity for operational efficiency improvements.
Low Priority	Observations rated "*low priority*" are not critical for the business unit, but should be addressed to either improve internal controls or minor operational efficiency opportunities.

HRZ-Staff-19

ATTACHMENT 4 – Synergy Savings Review, dated February 2019

Synergy Savings Review
Q3-Q4 2018

Internal Audit Department

February 2019

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EXECUTIVE SUMMARY

As part of our 2019 Internal Audit Plan, we recently completed a review of the synergy savings and transition costs captured in Q3-Q4 2018. The audit approach was discussed with management, and testing completed for the six month period July through December 2018.

The purpose of the review was to determine whether synergy savings and transition costs, incurred since June 30, 2018, had been accurately reported as at December 31, 2018.

The scope of the audit consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Understand the process used by People Services, Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including a review of any automated reports or spreadsheets used and ensuring consistency with past practices
- Validate operating and capital synergies and costs reported
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the monthly reports represent all costs incurred relating to merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

After a review of the process and supporting information, no material errors were noted. Internal Audit has identified the following areas requiring further management attention:

1. Severance Information
2. Minor Reporting Differences

In general, there continue to be controls in place to manage the synergy savings and transition costs reporting process. Many recommended courses of action from prior audits have already been put into place or are in the process of being implemented.

Overall assessment: Effective, with opportunity for improvement

1. Introduction

As a result of the merger between Enersource Inc., Horizon Utilities Inc. and PowerStream Inc., coupled with the acquisition of Hydro One Brampton Networks Inc., Alectra Utilities Inc. was formed. The main premise was to provide greater savings and allow the combined resources to take advantage of key strengths and maximize synergies. The synergies were quantified and presented in a business case against which Internal Audit was asked to conduct their review. This audit focused on information submitted from the end of the last audit, covering the period July 1, 2018 to December 31, 2018.

2. Audit Objective

As part of our internal audit plan, we recently completed a review of the synergy savings and transition cost recording process. The purpose of the review was to determine whether synergy savings and transition costs were accurately reported for the six month period ending December 31, 2018.

The audit plan was discussed with management, and testing completed for the period covering July 1 through December 31, 2018. Our approach consisted of the following steps:

- Interviews with management in identifying how the numbers were generated
- Review of the process involved
- Review of source documents
- Recalculation of material dollar amounts

3. Audit Scope

The scope of the review consisted of:

- Review detailed synergy savings and transition costs contained in the business case
- Understand the process used by the People Services, Finance and the Integration Management Office (IMO) teams to track and report on synergy savings and transition costs, including a review of any automated reports or spreadsheets used and ensuring consistency with past practices
- Review operating and capital synergies achieved in the monthly report
- Ensure that synergy savings are not offset by other expenses incurred
- Validate that transition costs in the monthly reports represent all costs incurred relating to the merger integration
- Review assumptions made by the IMO to ensure they are reasonable and consistently applied

The financial results for the months July through December 2018 were reviewed.

4. Client Accomplishments

The IMO, People Services and Finance have been working diligently to improve and streamline all facets of the reporting process and as a result, the reporting of monthly synergies and costs has greatly improved. This included rolling out new enhancements to the IMO headcount report that is shared with each business unit. On this report, they can see actual detailed headcount, position mapping and its link to the People Services' database.

The teams have implemented the recommendations from prior Internal Audit reviews and incorporated them into their processes. This included documenting processes and procedures and ensuring reporting would continue smoothly as a result. It should also be noted that the IMO has validated all labour savings with the affected business units. They have worked tirelessly to ensure that all requests for information were provided in a timely manner to ensure the audit process went smoothly.

5. Key Observations and Recommendations

Recommendations were developed through discussions with the Integration Management Office (IMO), Finance and People Services, along with results from detailed testing.

Observation #1 **Priority: Medium**	**Severance Information**
	During our mid-year review of the severance information, we noted that Non-Synergy information was being reported as well. It appeared that this had been corrected for the year end, as the spreadsheet had been locked and secured to not show non-synergy related severance. However, when simply copying the information from one Excel Spreadsheet to another, all of the synergy and non-synergy information became readily available. The risk is that sensitive and confidential information like severance amounts are not adequately safeguarded, resulting in the information being shared throughout the organization. In addition, during our review of the severance documents, we noted a minor discrepancy in tracking the amount of severance and its duration for one employee, resulting in a $27K discrepancy. Errors in severance documents could create an opportunity for legal disputes and controversy.
Recommendation	We recommend that the severance information be secured further or reported under separate cover if possible. Additional security measures should be installed to ensure that this information can only be viewed by those who require it. In addition, it is recommended the discrepancies are reviewed and corrected by People Services and Finance.
Response from Management	People Services will maintain two separate workbooks for the purposes of tracking synergy and non-synergy related severance costs, and only share the synergy related severance workbook with the IMO. This will ensure the full confidentiality of non-synergy related severances.
	Accountable Party: Boukette Pezzin Manager, People Services
	Estimated implementation date: March 12, 2019

<table>
<tr><td rowspan="2">Observation #2
Priority: Low</td><td>Minor Reporting Differences</td></tr>
<tr><td>During our review of the year-end report, we noted that the following minor discrepancies:

• Operating Locate Synergies– These were overstated on the year end IMO report due to an error in reporting the 2017 adjustment. The adjustment was to account for additional Check Box Clears related to locate synergies that was underreported in 2017. The amount reported should have been $349K but in error was reported as $385K, resulting in an overstatement of $36K;

• Capital Transition Costs – There were minor variances in the totals reported on the IMO report compared the support provided for ERP and Load Profiling & Settlement System Convergence costs, resulting in a net understatement of $5K.</td></tr>
<tr><td>Recommendation</td><td>We recommend that these amounts be adjusted in the next period.</td></tr>
<tr><td rowspan="3">Response from Management</td><td>The IMO will implement the required adjustments for the February reporting period.</td></tr>
<tr><td>Accountable Party:
Garen Boduryan
Manager Integration Reporting</td></tr>
<tr><td>Estimated implementation date:
March 12, 2019</td></tr>
</table>

6. Overall Assessment

It is important to note that Internal Audit reviewed actual values and did not review forecasted information prepared by IMO.

Internal Audit has identified some recommendations for improvements in the process. This audit has been rated as **'*Effective, with opportunity for improvement*.'**

7. Acknowledgement of Review

Name and Title	Signature	Date
Garen Boduryan, Manager, Integration Reporting		Feb 20/19
Boukette Pezzin Manager, People Services		Feb. 20/19
Barb Gray, SVP, People and Safety	Barb Gray	Feb 21/19

APPENDIX A: Synergies vs. 2017 Business Case

Internal Audit reviewed the synergies reported vs. the 2017 Business Case. It was noted that IMO relies on the individual business units and People Services to provide their input and validate reports.

Labour Synergies

The December 2018 Labour Synergies reported vs. the 2017 Business Case are as follows:

OM&A Net Savings	$ 16,662,193
Capital Labour Net Savings	$ 1,679,496
Total Net Savings	**$ 18,341,689**
Business Case	$ 16,353,047
Variance	**$ 1,998,642**
Vacant-Redundant Positions	150
Avoided Headcount Positions	21
Total Net Headcount Reductions	171
Business Case	128
Variance	**43**

150 positions were deemed vacant-redundant as at December, 2018, in addition to 21 avoided headcounts, totalling 171 net headcount reductions. This is favourable to the 128 predicted in the Business Case, giving a positive variance of 43 headcount. Per the IMO, this is the result of people deciding to leave earlier, through VSPs, or other reasons than noted in the 2017 Business Case.

Net Capital Synergies

The December 2018 Net Capital Synergies reported vs. the 2017 Business Case are as follows:

Net Capital Synergies	**$ 112,218**
Business Case	$ 2,140,775
Variance	**$ -2,028,557**

Higher capital transition costs are offset by the early recognition of HOBNI CIS replacement synergies, planned for in the 2019 and 2020 budget ($22M). The decision to recognize these savings earlier than planned was corroborated through the 2019 capital planning process, which validated the removal of these projects from the plan.

Net Operating Synergies

The December 2018 Net Operating Synergies reported vs. the 2017 Business Case are as follows:

Net Operating Synergies	**$ 32,475,161**
Business Case	$ 26,603,093
Variance	**$ 5,872,068**

APPENDIX B: Risk Rating Key

The following findings rating system has been established for evaluating the urgency of recommendations to be addressed:

Classification	Definition
High	• A significant breakdown in the control environment (i.e. process, controls); • Important issues are identified that could negatively impact the achievement of operational objectives; or • A legal non-compliance that could result in prosecution or significant penalty.
Medium	• A moderate breakdown in the control environment (i.e. process, controls); • Issues are identified that could negatively impact the efficiency and effectiveness of operations; or • A legal non-compliance that could result in an order, fine or notice of violation.
Low	• A minor breakdown in the control environment (i.e. process, controls) that on its own may have minimal impact but combined with other findings or left unattended has the potential to escalate; • Issues identified are less significant but opportunities that could enhance operations exists; or • A legal non-compliance that is administrative in nature and unlikely to escalate to something more serious.