

ONTARIO ENERGY BOARD

**HYDRO ONE NETWORKS INC.
ORILLIA POWER DISTRIBUTION CORPORATION**

**APPLICATION FOR APPROVAL TO PURCHASE ALL ISSUED AND OUTSTANDING
SHARES OF ORILLIA POWER DISTRIBUTION CORPORATION**

ORILLIA POWER'S ARGUMENT IN CHIEF

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I. Introduction

1. Orillia Power Distribution Corporation (“Orillia Power” or “OPDC”) provides these written submissions pursuant to Procedural Order No. 9 as its argument in chief in support of the application filed on September 26, 2018 under section 86(2) of the *Ontario Energy Board Act*, requesting approval for Hydro One Networks Inc. (“Hydro One”) to purchase all of the shares of Orillia Power (the “Transaction”) (the “MAADs Application”).
2. Orillia Power submits that this MAADs Application meets the no harm test set out by the Board in its previous decisions and that the Board should approve the Transaction.
3. The starting point for these submissions is the OEB’s decision in EB-2016-0276 where the OEB declined to approve the Transaction on the basis that no evidence was filed by Hydro One that Hydro One’s overall cost structure to serve Orillia Power’s customers will be no higher than Orillia Power’s underlying cost structure would have been absent the proposed acquisition in year 11. The Board wrote in that decision:

The OEB’s primary concern is that there is a reasonable expectation that underlying cost structures for the acquired utility are no higher than they would have been had the consolidation not occurred. Although the OEB accepts that the acquisition will lead to some savings on account of eliminating redundancies, that does not necessarily mean that Hydro One’s overall cost structure to serve Orillia’s customers will be no higher than Orillia’s underlying cost structure would have been absent the proposed acquisition.¹

4. In EB-2016-0276, the Board wanted to see a forecast of the costs to service Orillia customers beyond the ten year period and an explanation of the general methodology of how costs would be allocated to Orillia ratepayers after the deferral period.

The OEB is of the view that it would have been reasonable to see a forecast of costs to service Orillia customers beyond the ten year period and an explanation of the general methodology of how costs would be allocated to Orillia ratepayers after the deferral period. Hydro One takes the position that this information is not known. The OEB recognizes that any forecast of cost structures and cost

¹ EB-2016-0276 at page 12.

allocation 10 years out would include various assumptions and could not be expected to be 100% accurate. However, the OEB has highlighted its concern and its need to better understand the implications of how Orillia customers will be impacted by the consolidation beyond the ten year period. In the absence of information to address that OEB concern, the OEB cannot reach the conclusion that there will be no harm.

5. For this Application, Hydro One and Orillia Power have been responsive to the Board's concerns and filed evidence demonstrating that the overall cost structure beyond the deferral period is expected to be lower than if there was no Transaction. This evidence was subject to numerous interrogatories, a two-day Technical Conference and withstood cross-examination over a two-day oral hearing. None of the interveners or Board Staff undermined the reasonability of the forecasts provided by Hydro One and Orillia Power. As such the Application and the Transaction should be approved.
6. In EB-2016-0276, the Board found that all other components of the no harm test had been satisfied except for the forecast of cost structures in the eleventh year.
7. As the evidence on this application is similar to that provided in EB-2016-0276, with the exception of the forecasts for the eleventh year, Orillia Power submits that the only live issue is whether the forecasts presented by Hydro One and Orillia Power are reasonable and whether those forecasts meet the no harm test.

II. The No Harm Test

8. Section 86 of the *Ontario Energy Board Act*, 19981 (the "Act") requires that the OEB review applications for a merger, acquisition, divestiture or amalgamation that result in a change of ownership or control of an electricity transmitter or distributor and approve applications which are in the public interest.
9. The OEB applies the no harm test in its assessment of consolidation applications, as described in *The Handbook to Electricity Distributor and Transmitter Consolidations* (Handbook) issued by the OEB on January 19, 2016.
10. The OEB considers whether the no harm test is satisfied based on an assessment of the cumulative effect of the transaction on the attainment of its statutory objectives. If the

proposed transaction has a positive or neutral effect on the attainment of these objectives, the OEB will approve the application.

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

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

1.1 To promote the education of consumers.

2 To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.

3. To promote electricity conservation and demand management in a manner consistent with the policies of the Government of Ontario.

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

5. To promote the use and generation of electricity from renewable energy sources in a manner consistent with the policies of the Government of Ontario, including the timely expansion or reinforcement of transmission systems and distribution systems to accommodate the connection of renewable energy generation facilities.

12. The leading case on the no harm test is the Board's Decision and Order in EB-2016-025/EB-2016-0360 dated December 8, 2016 in respect of the merger of utilities that would eventually become known as Alectra Utilities (the "Alectra Decision").

13. In the Alectra Decision, the Board provided additional guidance on the no-harm test at pages 5 and 6:

While the OEB has broad statutory objectives, in applying the no harm test, the OEB's review primarily focuses on the impacts of the proposed transaction on price and quality of service to customers, and the cost effectiveness, economic efficiency and financial viability of the consolidating utilities. The OEB considers this an

appropriate approach, given the performance-based regulatory framework under which regulated entities are required to operate and the OEB's existing performance monitoring framework.

The OEB has implemented a number of instruments, such as codes and licences that ensure regulated utilities continue to meet their obligations with respect to the OEB's statutory objectives relating to conservation and demand management, implementation of smart grid, and the use and generation of electricity from renewable resources. With these tools and the existing performance monitoring framework, the OEB is satisfied that the attainment of these objectives will not be adversely affected by a consolidation and the no harm test will be met following a consolidation.²

III. Background on Orillia Power

14. Orillia Power is a wholly owned subsidiary of Orillia Power Corporation ("OPC"). OPC is a holding company, currently wholly owned by The Corporation of the City of Orillia (the "City").
15. The City and OPC (together, the "Vendor") entered into a share purchase agreement the effect of which is that the Vendor agreed to sell and Hydro One Inc. has agreed to purchase all of the issued and outstanding shares of OPDC.

IV. Price, Cost Effectiveness and Economic Efficiency

A. Introduction

16. The Handbook states that to demonstrate no harm, applicants must show that there is a reasonable expectation based on underlying cost structures that the costs to serve customers following a consolidation will be no higher than they would otherwise have been.
17. Orillia Power submits that the effect of consolidation on underlying cost structures will be positive, that costs to serve customers will be no higher because of the consolidation and that consolidation will have a positive effect on economic efficiency and cost effectiveness.

² Alectra Decision EB-2016-0025 and EB-2016-0360 at pages 5-6.

B. Orillia's Evidence with respect to the 10th and 11th years

18. In these submissions, Orillia Power discusses how its forecasts are reasonable and the evidence underlying those forecasts.
19. Orillia Power provided forecasts at Attachment 18 to the Application of its Revenue Requirements for Year 10 and Year 11, being 2030.
20. Orillia Power's witnesses were cross-examined on those forecasts during the oral hearing and their evidence and forecasts withstood cross-examination. In particular, OEB Staff, cross-examined Mr. Hurley at Orillia Power on Attachment 18:
 - (a) Mr. Hurley explained that Orillia Power has not re-based since 2010. Mr. Hurley testified that at the 2010 rate hearing, Orillia power obtained very favourable cost of capital parameters that have enabled them to keep revenues at reasonable levels.³
 - (b) Orillia Power has capital expenditures of about \$3 million a year on average;⁴
 - (c) When preparing the forecast, Orillia Power relied upon a projection for their 5 year capital plan and then for the next 5- 6 years, Orillia Power relied upon the average spending from previous years;⁵
 - (d) OM&A escalated by CPI of about 2%.⁶
21. Orillia Power also noted, and this is significant, that for the last three years, since they entered into the Share Purchase Agreement with Hydro One Inc., Orillia Power has, in some respects, been on hold (for example, by not applying for annual IRM adjustments).

³ Transcript Day 2 at page 62 and page 169.

⁴ Transcript Day 2 at page 63

⁵ Transcript Day 2 at page 63

⁶ Transcript Day 2 at page 63

As a result, Orillia Power, among other things, has lost staff along with other consequences. If the Transaction is not approved, Orillia Power will need to replenish those staff numbers.

22. As such, when looking at Orillia Power's current financial situation, it must be taken into account that Orillia Power's current cost structures are artificially low which will not continue going forward given that ⁷ Orillia Power must rebase going forward to restore their revenue against their cost structure.⁸
23. The Board should accept Orillia Power's forecasts for the tenth and eleventh year for the status quo as reasonable. Those forecasts withstood cross-examination and there has been no evidence presented by any party that Orillia's forecasts are unreasonable.

C. Cost Structures and Revenue Requirements in Year 10 and 11

24. The following table and forecasts are based on the forecasts provided by Orillia Power and Hydro One. These are forecasts and must be reviewed on a standard of reasonableness. The Board must be satisfied that the forecasts provided by Orillia Power and Hydro One are reasonable. It is not a standard of perfection or certainty. As the Board held in Alectra: "the estimates must be sufficiently accurate for the purposes of the analysis under the no harm test." ⁹
25. The Application demonstrates that the cost structures from proceeding with the transaction will result in expected ongoing operations, maintenance and administrative (OM&A) savings. In particular, Hydro One projects OM&A savings of \$4.7 million in year 10 after consolidation.¹⁰
26. As a result of these types of savings, it is anticipated that the revenue requirement per Orillia Power customer for the three rate classes will be significantly lower with consolidation than without consolidation in year 11. The following table responding to

⁷ Transcript Day 2 at page 169.

⁸ Transcript Day 2 at page 169.

⁹ Alectra Decision at page 12.

¹⁰ Response to Undertakings JT2.11 Attachment 2.

Staff Interrogatory #12 on which Hydro One and Orillia Power were cross-examined is illustrative of this savings¹¹:

| OPDC | Today | Year 10 (2029) With consolidation | Year 10 (2029) Without consolidation | Year 11 (2030) With consolidation | Year 11 (2030) Without consolidation |
|---|---------------------|--|---|--|---|
| Revenue Requirement per Customer | | | | | |
| Residential | \$357 | \$356 | \$518 | \$366 | \$526 |
| GS < 50 kW | \$1,155 | \$1,162 | \$1,699 | \$997 | \$1,726 |
| GS 50-4,9999 kW | \$14,430 | \$14,958 | \$21,234 | \$13,241 | \$21,587 |
| Other | \$90 | \$95 | \$143 | \$140 | \$146 |
| <u>Total</u> | <u>\$489</u> | <u>\$496</u> | <u>\$719</u> | <u>\$485</u> | <u>\$731</u> |

27. A similar table has been submitted into evidence with respect to the effects on existing Hydro One customers that considers the scenarios of revenue per customer with or without consolidation. This table demonstrates that Hydro One legacy customers will be no worse off following consolidation in year 11. This was subject to thorough cross-examination by SEC and withstood cross-examination.

D. Additional Factors with respect to the no-harm test

28. Orillia Power customers will also benefit from a 1% reduction in base distribution rates following the transaction, and these reduced rates will be frozen over a five-year period.¹² From years 6 to 10, Orillia Power customers' rates will then be set using the Price Cap adjustment mechanism, as outlined in the Board's Report "*Rate Making Associated with Distribution Consolidation*".

¹¹ Compendium for SEC Cross-Examination, OEB Staff Interrogatory #12, SEC Compendium at page 5.

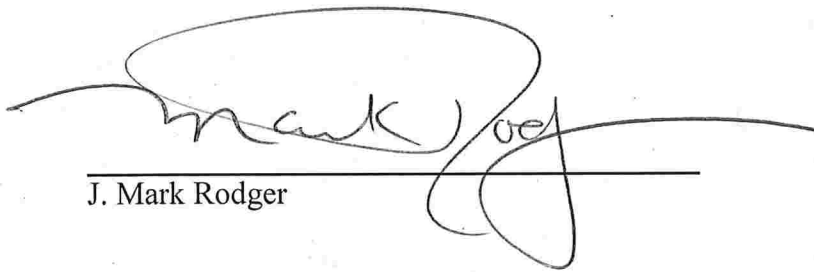
¹² Exhibit A, Tab 1, Schedule 1, page 3, Footnote 2.

29. At the commencement of year six, Hydro One will apply the OEB's Price Cap Index formula utilizing the former OPDC's efficiency cohort factor of 0.30%. This will be anchored to then current OPDC Base Distribution Rates, and applied annually.¹³ In addition, the guaranteed ESM removes 100% of the risk of Hydro One obtaining the savings from OPDC's ratepayers.
30. Orillia Power customers will benefit from increasing economies of scale that will be of benefit to them in the long term.

V. Conclusion

31. Orillia Power submits that the Board should approve the Application. The Applicants have discharged their burden of demonstrating that the cost structures in years 10 and 11 will be no higher than they would be under the status quo for both Orillia Power and Hydro One. As such, the evidence demonstrates that the Transaction has no adverse impact on price, adequacy, reliability and quality of electricity service of Orillia Power and Hydro One.

All of which is respectfully submitted, December 13, 2019



J. Mark Rodger

¹³ Applicator at page 7 of 25.