

**SCOTT POLLOCK**  
T 613.787.3541  
spollock@blg.com

Borden Ladner Gervais LLP  
World Exchange Plaza  
100 Queen St, Suite 1300  
Ottawa, ON, Canada K1P 1J9  
T 613.237.5160  
F 613.230.8842  
blg.com



Our File No. 339583-00264

**By electronic filing**

December 16, 2019

Christine Long  
Registrar and Board Secretary  
Ontario Energy Board  
2300 Yonge Street, Suite 2701  
Toronto ON M4P 1E4

Dear Ms. Long

**Re: Hydro One Networks Inc. (“Hydro One”)  
Application for 2020-2022 Transmission Rates  
Board File No.: EB-2019-0082**

Please find attached the Submissions of Canadian Manufacturers & Exporters (“CME”) in the above-noted proceeding.

Yours very truly

**Borden Ladner Gervais LLP**

A handwritten signature in blue ink, appearing to read 'Scott Pollock', is written over a light blue horizontal line.

Scott Pollock

Encl.

- c. Linda Gibbons and Frank D’Andrea (Hydro One)
- Charles Keizer and Arlen Sternberg (Torys LLP)
- EB-2019-0082 Intervenors
- Alex Greco (CME)

OTT01: 10218206: v1

**ONTARIO ENERGY BOARD**

**Hydro One Networks Inc.**

Application for Electricity Transmission Rates Beginning  
January 1, 2020 Until December 31, 2022

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**SUBMISSIONS OF  
CANADIAN MANUFACTURERS & EXPORTERS (“CME”)**

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**December 16, 2019**

Emma Blanchard  
Erin Durant  
Scott Pollock  
Borden Ladner Gervais LLP  
World Exchange Plaza  
100 Queen Street, Suite 1300  
Ottawa, ON K1P 1J9  
  
Counsel to CME

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## 1.0 INTRODUCTION

1. These submissions are made on behalf of Canadian Manufacturers & Exporters (“**CME**”).
2. CME’s members include over 400 Ontario based companies that operate energy intensive businesses. Their continued competitiveness in their respective industries is tied directly to energy costs and, as a result, the dramatically increasing cost of energy in Ontario has made it much more difficult for CME members to be competitive in the market, compared with businesses in other jurisdictions where energy costs less.
3. Hydro One Networks Inc. (“**HONI**”) has proposed a rate-setting framework for their transmission business for three years commencing January 1, 2020. It requests approval for revenue requirements of \$1,596 million in 2020, \$1,677.4 million in 2021 and \$1,773.2 million 2022.<sup>1</sup> These increases to the revenue requirement will drive transmission rate increases of 6.6%, 5.7% and 6.4%, over the course of 2020-2022 respectively.<sup>2</sup> Accordingly, they will be a significant driver of energy costs for CME members for the entirety of the plan term.
4. In preparing these submissions, CME has benefitted from reviewing both Board Staff’s and School Energy Coalition’s (“**SEC**”) submissions. This has assisted CME in making efficient use of resources given the scope of this application.
5. These submissions focus on the components of the Applicant’s proposal that in CME’s submission, require adjustment in order to ensure rates in Ontario are just and reasonable, and to protect ratepayers with respect to the cost of electricity transmission. Where these submissions do not touch on an issue that was outlined in the Board’s approved issues list, CME takes no position with respect to that issue.

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<sup>1</sup> EB-2019-0082, Exhibit J1.1, Table 8.

<sup>2</sup> EB-2019-0082, Exhibit J1.1, Table 8.

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## 2.0 THE APPLICATION

6. On March 21, 2019, HONI filed an application for an order approving just and reasonable rates and other charges for electricity transmission to be effective January 1, 2020 to December 31, 2022 (the “**Application**”) pursuant to section 78 of the *Ontario Energy Board Act, 1998* (the “**OEB Act**”).<sup>3</sup>
7. On June 19, 2019, HONI updated substantial portions of their evidence.
8. A technical conference was held on August 12 and 13, 2019, and nine days of oral hearing were held from October 21 to November 4, 2019.
9. On August 21, 2019, the Ontario Energy Board (“**OEB**” or the “**Board**”) released Procedural Order No. 3, wherein the Board stated that submissions would be due on the following dates: HONI’s Argument-in-Chief on November 22, 2019, OEB Staff submissions on December 11, 2019, intervenor submissions on December 16, 2019, and HONI’s reply on January 17, 2020.
10. The Application proposes the following:
  - To set rates for 2020 through a cost of service forward test year approach, as well as a revenue cap mechanism to set rates during the rest of the plan period. The revenue cap proposal features an  $I - X$  formula for increasing rates and a stretch factor of 0% set for all subsequent years of the plan term;<sup>4</sup>
  - To increase rates by an average of 6.2%, for the 2020-2022 period;<sup>5</sup>
  - To provide \$370 million in up-front productivity savings;<sup>6</sup>
  - An earnings sharing mechanism (“**ESM**”) that would share any earnings above a 100 basis point dead-band with ratepayers on a 50/50 basis;

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<sup>3</sup> *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15 Sched B.

<sup>4</sup> EB-2019-0092, Transcript, Vol. 1, p. 13, lines 3-8.

<sup>5</sup> EB-2019-0082, Exhibit J1.1, Table 8. Derived from the simple average of 6.6%, 5.7% and 6.4% which are the listed transmission increases as of the oral hearing update.

<sup>6</sup> EB-2019-0082, Exhibit K1.1, Hydro One 2020-2022 Transmission Revenue Requirement Application Overview, October 21, 2019, p. 8.

- A custom capital or “C” factor, that would escalate rates based on projected revenue requirement impacts resulting from planned increases in rate base during the plan term;
- A “Z” factor with a materiality threshold of \$3 million; and
- A Capital In-Service Variance Account that tracks the difference between the revenue requirement associated with actual in-service capital additions during the rate year and the corresponding revenue requirement associated with the OEB-approved in-service capital additions. HONI proposes that if their actual cumulative in-service additions are 98% or less of the forecast amounts, the difference will be recorded in the variance account and returned to ratepayers.

### 3.0 CUSTOM APPLICATION

#### 3.1 Inflation and Productivity Factors

##### 3.1.1 Inflation Factor

11. As part of its custom rate-making application, HONI proposes to use an electricity transmission industry-specific inflation measure similar to the one the Board approved in the Hydro One Sault St. Marie proceeding (EB-2018-0218) (the “**HOSSM Proceeding**”).
12. The growth in HONI’s proposed inflation measure would be a weighted average of the growth in Canada’s gross domestic product implicit price index for final domestic demand (“**GDP-IPI-FDD Canada**”) and the average weekly earnings for workers in Ontario (“**AWE Ontario**”).<sup>7</sup> The GDP-IPI-FDD Canada would be weighted at 86%, and the AWE Ontario at 14%.<sup>8</sup>

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<sup>7</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 14 of 76.

<sup>8</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 14 of 76.

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13. HONI's proposal results in an inflation factor of 1.8%,<sup>9</sup> which HONI proposes to update annually as calculated and issued by the OEB.<sup>10</sup>
  14. In the HOSSM Proceeding, the Board determined that the two factor IPI, including weighting at 86% and 14% respectively, was appropriate, and consistent with the Board's previous decisions applicable to electricity distributors, Ontario Power Generation Inc. ("**OPG**"), and electricity transmitters.<sup>11</sup>
  15. Accordingly, CME submits that HONI's proposal regarding the inflation factor is appropriate.

### **3.1.2 Electricity Transmission Industry Productivity Results**

16. HONI hired Power Systems Engineering, Inc. ("**PSE**") to conduct a total factor productivity study for its transmission system and a custom econometric benchmarking study of its total transmission costs (the "**PSE Report**"). PSE's report was largely the same as the one HONI filed in the HOSSM Proceeding.
17. The PSE Report, filed with HONI's application on March 21, 2019, found that the industry wide productivity trend for electricity transmitters was -1.45% from 2004-2016.<sup>12</sup> PSE found that HONI's growth rate had been better than the industry wide trend at -0.18% during the sample period, but forecast that HONI's productivity would fall to -1.70% during the incentive rate period.<sup>13</sup>
18. In recognition of the fact that the Board has not previously recognized negative industry-wide productivity factors, PSE proposed an industry-wide productivity factor of 0%.<sup>14</sup>
19. On September 5, 2019, Pacific Economics Group Research LLC ("**PEG**") also submitted a report analyzing electricity transmitter productivity trends (the "**PEG Report**"). PEG's

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<sup>9</sup> EB-2019-0082, Transcript, Vol. 8, p. 18, lines 15-21.

<sup>10</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, pp. 4 and 5 of 13.

<sup>11</sup> EB-2018-0218, Decision and Order, June 20, 2019, p. 16.

<sup>12</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, Attachment 1, p. 11 of 59.

<sup>13</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, Attachment 1, p. 11 of 59.

<sup>14</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 14 of 76.



methodology varied from PSE's in a number of respects. While the PSE Report used data from 2005 to 2016,<sup>15</sup> PEG's determined that a longer period was appropriate for the study. During the full period of PEG's study (1996-2016), PEG found that the transmission industry productivity declined at a much more modest rate of -0.25% per year.<sup>16</sup>

20. On October 15, 2019, HONI filed a reply report from PSE (the "**PSE Reply Report**"), which replied to PEG's critique of its original report, and updated its evidence to include data from 2017 and 2018. The PSE Reply Report stated that the base productivity trend for the electricity transmission industry was -1.61%.<sup>17</sup> PSE's recommendation regarding the base productivity factor of 0% remained unchanged.
21. While there are important methodological differences between PSE and PEG regarding how best to calculate the industry-wide productivity trend, given that both PSE and PEG concluded that the trend was negative, CME agrees with HONI's proposed 0% industry-wide productivity factor, and submits that 0% is in keeping with the Board's previous directions, and appropriate under the circumstances.

### **3.1.3 Stretch Factor**

22. CME disagrees with HONI's proposal to have a 0% stretch factor, and submits that the Board should apply a .3% stretch factor instead.
23. PSE's conducted a total cost-benchmarking analysis as part of the PSE Report. PSE employed an econometric method, whereby certain chosen variables were fed into a model and the model predicts what costs a utility, sharing HONI's unique characteristics, should have. Those model costs are then compared to HONI's actual costs. To the extent that HONI's actual costs are below those of the model, HONI would be considered a

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<sup>15</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 8 of 76.

<sup>16</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 8 of 76.

<sup>17</sup> EB-2019-0082, Reply to PEG's Report ("Incentive Regulation for Hydro One Transmission"), Power System Engineering, Inc., October 15, 2019, p. 6.

- superior cost performer. To the extent that HONI's actual costs are above the model's prediction, HONI would be considered an inferior cost performer.
24. PSE concluded that HONI's projected costs for 2020-2022 were 27.1% less than PSE's model would expect.<sup>18</sup> As a result, PSE opined that the appropriate stretch factor for HONI was 0%.<sup>19</sup>
25. PEG also completed a cost benchmarking analysis for HONI. In its report, PEG was critical of PSE's methodology in a number of respects, including PSE's choice of sample size, the use of U.S. inflation indexes instead of Ontario indexes, and other concerns, such as regional price levelization.<sup>20</sup>
26. In contrast to PSE's conclusion, PEG found that HONI's cost performance had deteriorated in recent years. Whereas HONI's cost was found to be about 2.1% below the model's prediction on average between 2014-2016, HONI was above the costs predicted by PEG's model during the 2020-2022 period by 6.8%.<sup>21</sup> Accordingly, PEG recommended a stretch factor of 0.3%.
27. PSE's Reply Report argued that areas criticized by PEG were inconsequential to the result.<sup>22</sup> PSE also contended that PEG's report was itself flawed in two ways: first, that PEG's research was biased against the more recent and forecast years of the sample; and second, that PEG's modelling procedure was not accessible and transparent.<sup>23</sup>
28. As will appear below, PEG's report provides a more accurate and robust calculation of HONI's cost benchmarking performance. Accordingly, CME submits that the Board should apply a .3% stretch factor to HONI during the custom IR term commensurate with PEG's findings.

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<sup>18</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, Attachment 1, p. 10 of 59.

<sup>19</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, Attachment 1, p. 14 of 59.

<sup>20</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, pp. 23-24 of 76.

<sup>21</sup> EB-2019-0082, Exhibit M1, p. 9. PEG's original finding of 9% was then updated to reflect HONI's cost performance as being 6.8% above model predictions. See Transcript, p. 131 line 20-24.

<sup>22</sup> EB-2019-0082, Reply to PEG's Report ("Incentive Regulation for Hydro One Transmission"), Power System Engineering, Inc., October 15, 2019, s. 3.2.

<sup>23</sup> EB-2019-0082, Reply to PEG's Report ("Incentive Regulation for Hydro One Transmission"), Power System Engineering, Inc., October 15, 2019, ss. 1.1.1, 1.1.2.

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**3.1.3.1 A Longer Sample Period is to be Preferred**

29. As part of their respective econometric analyses, both PEG and PSE used data from a variety of other entities over a number of years in order to calibrate the econometric cost model. PSE originally selected 2004-2016 as their time period (later updated to 2004-2018), whereas PEG selected 1995-2016 as their time period.<sup>24</sup>
30. CME submits that the longer sample period chosen by PEG is to be preferred.
31. Statistically, longer time periods with more data provide more accurate results. This fact is equally true regarding econometric analyses, where the inclusion of further data allows for a more accurate and precise econometric model.<sup>25</sup> While CME commends PSE for updating the model to include 2017 and 2018 data, PSE's 14-year time frame still does not provide as robust a data set as that provided by PEG's sample.
32. Furthermore, PSE's chosen sample period produces a material trend variable parameter of 0.012.<sup>26</sup> As outlined by Dr. Lowry, this parameter allows benchmarked costs to grow by 1.2% annually for reasons that have nothing to do with the changes in the values of the model's business condition variables.<sup>27</sup> In other words, this parameter provides HONI with a significant year-over-year cost cushion with respect to its performance against the model that is outside of the variables used in the model.

**3.1.3.2 The Use of Ontario Indexes are to be Preferred**

33. As part of its analysis, PSE used U.S. inflation indexes that they adjusted for the purchasing power parity between the United States and Canada. This included U.S. employment cost indexes. In contrast, PEG employed Canadian indexes such as the implicit capital stock deflator for the Canadian utility sector and AWE of Ontario workers.<sup>28</sup>

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<sup>24</sup> PEG was unable to update their calculations to include 2017 and 2018 prior to the EB-2018-0082 hearing.

<sup>25</sup> EB-2018-0082, Transcript, Vol. 9, p. 47, lines 15-22.

<sup>26</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 22 of 76.

<sup>27</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 22 of 76.

<sup>28</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 23 of 76.

34. CME submits that Canadian indexes should be preferred when calculating HONI's cost performance. The actual inflationary pressures that HONI faces are, quite naturally, Canadian.
35. For instance, the amount of inflation that HONI must face in the labour market is most accurately captured by the average weekly earnings measure for Ontario. The Board explicitly recognizes this fact, as the AWE Ontario is the measure that the Board has favoured when setting the inflation factor as part of the I – X rate-setting regime.
36. As outlined by Dr. Lowry, the United States indexes could exaggerate the rate of construction cost growth as compared to their Canadian counterparts.<sup>29</sup> As a result of this disconnect, PSE's methodology assumes that more of HONI's cost growth has been due to input price inflation than it actually has. Critically, this assumed inflation is not reflective of the actual inflation that has taken place in Ontario – where HONI purchases its capital stock, and from which it draws its labour.
37. Accordingly, CME submits that the most appropriate inflation indexes to use are those reflective of Canadian and Ontario markets, not unrelated U.S. jurisdictions.

**3.1.3.3 PSE's Cost Levellizing for Headquarter Cities is Inappropriate**

38. PSE included regional input prices into their model in order to adjust the econometric model's cost predictions to take into account the costs of local inputs.
39. The PSE Report states that this was accomplished by taking the:
- [S]imple average of the RSMeans index values for cities in the service territory.<sup>30</sup>***
40. Despite the statement above, the actual methodology used by PSE is to take the RSMeans index value for only the headquarter city. As stated by PSE in an interrogatory from the HOSSM proceeding:

<sup>29</sup> EB-2018-0082, Transcript, Vol. 9, p. 51, line 21 – p. 52 line 16.

<sup>30</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, Attachment 1, p. 31 of 59.

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***The city assigned to each utility in the sample for the RSMeans mapping, including Hydro One Networks, was based only on the headquarter city for each utility. In Hydro One Networks' case, this was Toronto.<sup>31</sup>***

41. Accordingly, each utility was only assigned one RSMeans score, and that score was from the city in which the utility's headquarters were located.
42. HONI's RSMeans score city was Toronto. According to Mr. Fenrick, Toronto has costs that are 12.3% higher than the average city RSMeans score.<sup>32</sup> This gives HONI a pronounced advantage when comparing HONI's costs to the model's prediction, as other utilities likely have headquarters that are located in cheaper cities.
43. Furthermore, HONI's service territory covers the entire province of Ontario. As a result, significant portions of HONI's costs will be incurred in smaller cities and regions in Ontario, regions where costs are not nearly as high as those in Toronto. As a result, HONI's regional input costs would be much lower on average than PSE's model expects, giving HONI an advantage during the cost benchmarking.
44. While PSE initially defended its choice to use Toronto's RSMeans score by stating that he believed it was a good approximation for HONI's overall costs,<sup>33</sup> on cross-examination, Mr. Fenrick admitted that he didn't actually know whether Toronto's RSMeans score was a good approximation or not.<sup>34</sup>
45. PSE also defends its choice of RSMeans score by stating that this methodological issue has a minor impact on the final cost benchmarking results, and that PEG's report uses the same methodology.
46. In this regard, CME notes that Mr. Fenrick pointed out the RSMeans levelization could influence the benchmarking results by as much as 2%.<sup>35</sup> Given the number of

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<sup>31</sup> EB-2018-0218, Exhibit I, Tab 1, Schedule 66, p. 1.

<sup>32</sup> EB-2019-0082, Transcript, Vol. 8, p. 8, line 25 – p. 9, line 7.

<sup>33</sup> EB-2019-0082, Reply to PEG's Report ("Incentive Regulation for Hydro One Transmission"), Power System Engineering, Inc., October 15, 2019, s. 3.2.8 (1).

<sup>34</sup> EB-2019-0082, Transcript, Vol. 8, p. 15, line 24 – p. 16, line 1.

<sup>35</sup> EB-2019-0082, Transcript, Vol. 8, p. 11, line 27 – p. 12, line 10.

methodological issues that have arisen between the experts in this proceeding, CME submits that even if they only changed the results by 2% each, that would quickly become a significant impact on HONI's cost benchmarking results.

47. Furthermore, CME agrees that PEG's methodology should also employ this approach to regional cost levelizing. This methodological improvement would cause HONI's results to deteriorate relative to PEG's findings as well.

#### **3.1.3.4 PEG's Model Does Not Disclose a Bias**

48. As part of the PSE Reply Report, PSE criticized PEG and concluded that PEG's model was biased against the later years in the sample period, as well as the forecast years to come. Specifically, PSE contended that PEG's model was calculating the benchmark scores of the entire utility sample to be inordinately high in the later years of the sample period, concluding at 15% higher in 2018.<sup>36</sup>
49. PEG's conclusion regarding this trend in their research confirms that their model is not biased, but in fact, models precisely the cost performance that has existed for the previous decade. As part of his examination-in-chief, Dr. Lowry explained that U.S. transmission productivity has declined since 2006, as the result of sweeping legislative changes that encouraged material growth in capital expenditures, as well as weakening cost containment.<sup>37</sup>
50. Critically, these changes cause cost performance to decline in the short-run. While PEG's model shows poor cost performance for the bulk of the sampled utilities for the past 10 years, that is precisely the impact that increased capital expenditures and reduced cost containment incentives would have.<sup>38</sup>

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<sup>36</sup> EB-2019-0082, Reply to PEG's Report ("Incentive Regulation for Hydro One Transmission"), Power System Engineering, Inc., October 15, 2019, p. 8.

<sup>37</sup> EB-2019-0082, Transcript, Vol. 9, p. 47, line 23 – p. 49, line 24.

<sup>38</sup> EB-2019-0082, Transcript, Vol. 9, p. 47, line 23 – p. 49, line 24.

51. Accordingly, far from being a criticism of PEG's report, CME submits that this demonstrates that PEG's methodology and explanations are in fact consistent with one another, and demonstrate a definite trend in cost performance in the U.S. sample utilities that were caused by external legislative and regulatory changes. These changes did not exist for HONI, and likely will not occur through the plan period.

**3.1.3.5 PEG's Modelling Process is an Improvement over EB-2018-0218**

52. PSE also criticized PEG's modelling process, which was not employed in the HOSSM Proceeding. Specifically, PSE criticized PEG's use of auto-correlation adjustments, as well as what it believes to be an unnecessarily opaque modelling technique that was difficult to replicate.<sup>39</sup>
53. With respect to the former criticism, PSE stated that the coefficients used in its cost-benchmarking analysis were unbiased, and could not be improved upon.<sup>40</sup> However, as explained by Dr. Lowry, while PSE's methodology addresses one issue with auto-correlation, namely the possible corruption of standard error statistics, it does not address the "efficiency" of the parameters estimates, which is their tendency to be scattered around the true value of the parameter.<sup>41</sup> Accordingly, when PSE states that its method cannot be improved upon, what PSE means is that the PEG and PSE's methods are equally unbiased, not that PSE's methodology cannot be improved upon in any respect.
54. Additionally, PSE used similar auto-correlation correction procedures in some of their own prior studies.<sup>42</sup> Accordingly, this criticism of PEG's work is unwarranted.
55. With respect to PSE's second criticism, PEG explained during direct examination that its auto-correlation correction procedure was a standard and widely accepted econometric

<sup>39</sup> EB-2019-0082, Reply to PEG's Report ("Incentive Regulation for Hydro One Transmission"), Power System Engineering, Inc., October 15, 2019, s. 1.1.2.

<sup>40</sup> EB-2019-0082, Transcript, Vol. 8, p. 166, lines 13-26.

<sup>41</sup> EB-2019-0082, Transcript, Vol. 9, p. 52, line 18 – p. 49, line 24.

<sup>42</sup> EB-2019-0082, Transcript, Vol. 9, p. 54, lines 14-27.

process. Moreover, popular statistical software packages contain function that allow the practitioner to replicate PEG's work and methodology.<sup>43</sup> Far from being opaque and unnecessary, PEG has demonstrated that their auto-correlation efforts not only improve the results provided by the model, but are also accessible.

56. Accordingly, CME submits that PSE's criticism of PEG's methodology is unwarranted. PEG's evidence shows that HONI is an average cost performer as an electricity transmitter, and therefore should be accorded a stretch factor commensurate with an average cost performer – 0.3%.

### **3.2 Capital Factor**

57. As part of their custom IR application, HONI has proposed the use of a capital or "C" factor, as part of the IR rate setting formula. In HONI's view, the C factor is necessary in order to recover the incremental revenue in each test year necessary to support HONI's Transmission System Plan ("TSP"), beyond the amount baked into rates through the normal I – X adjustment.<sup>44</sup>
58. In HONI's proposal, the C factor will drive the majority of the revenue requirement increases, which will then flow down to customers in the form of rate increases. While HONI forecasts inflation, or the "I" factor, in their pre-filed evidence as being around 1.8% annually for 2021 and 2022, the C factor is forecast to drive a 3.58% and 4.11% increase in the revenue cap in 2021 and 2022 respectively.<sup>45</sup>
59. CME submits that HONI's C factor should not be accepted as proposed. Instead, the Board should make several adjustments to the C factor, including:
- (a) Adding a supplementary stretch factor to ameliorate the C factor's impact on HONI's incentive to contain costs throughout the plan term; and
  - (b) Exclude working capital from the calculation of the C factor.

<sup>43</sup> EB-2019-0082, Transcript, Vol. 9, p. 54, line 28 – p. 55, line 10.

<sup>44</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, p. 6.

<sup>45</sup> EB-2019-0082, Exhibit J1.1, Table 3.



### **3.2.1 The C Factor Should Attract a Supplementary Stretch Factor**

60. The C factor proposed by HONI in this application is calculated as the percentage change in the total revenue requirement attributable to new capital investments that is not otherwise recovered from customers. In other words, the C factor represents a complete recovery of the amounts HONI forecasts to spend on new capital investments during the plan term that are not already paid for through the existing I – X mechanism.
61. As Dr. Lowry noted in his report,<sup>46</sup> the inclusion of a C factor, along with HONI's numerous variance accounts and the Z factor would mean that HONI's capital revenue would be established primarily on a cost of service basis.<sup>47</sup>
62. The disparity between how capital spending and OM&A are treated could lead to improper incentives for HONI during its plan term. As stated by Dr. Lowry during his testimony:

***“So, there is, in principle, a perverse incentive to spend money on capex in order to reduce the company's OM&A costs. And this violates the spirit of the Board's custom IR guidelines and all in all, I think it is actually debatable whether this regulatory system should be categorized as incentive ratemaking at all.”<sup>48</sup>***

63. The Board has also recognized the danger in previous applications. In EB-2017-0049, HONI distribution's last application, the Board determined that it would apply a supplementary stretch factor, recognizing the danger inherent in having capital expenditures be remunerated on a cost of service basis:

***“The OEB approves the approach to the capital factor as proposed by Hydro One, but imposes an additional 0.15% stretch factor to be subtracted from the calculated capital factor. This is in addition to the 0.45% stretch factor applied to the revenue requirement and the reductions to the capital program discussed under Issue 30.***

***PEG expressed concerns that with the capital factor the “Company is perversely incented to spend excessive amounts on capital to contain OM&A expenses”... the OEB has taken this recommendation into consideration in the adoption of the incremental stretch factor that will apply to the capital factor.”<sup>49</sup>***

<sup>46</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 41 of 76.

<sup>47</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 41 of 76.

<sup>48</sup> EB-2019-0082, Transcript, Vol. 9, p. 56, lines 15-20.

<sup>49</sup> EB-2017-0049, Decision and Order, March 7, 2019, pp. 31-33.

64. In order to ensure that HONI's incentives are properly aligned with ratepayer interests, and with the Board's intent as part of the Renewed Regulatory Framework ("RRF"), CME submits that the Board should apply a supplementary stretch factor similar to the one it approved in EB-2017-0049, calibrated at 0.15%. This supplementary stretch factor would be in addition to the stretch factor of .3%.
65. While PEG proposes a number of possible mechanisms which could be added to better align utility behavior with incentive regulation,<sup>50</sup> this area of incentive regulation is still fairly novel. Accordingly, CME suggests that the Board apply the .15% stretch factor, until a more comprehensive mechanism emerges to ensure that incentive ratemaking continues to incent the appropriate behavior from utilities.

### **3.2.2 Working Capital and the Calculation of the C Factor**

66. In its decision in EB-2017-0049, HONI's most recent rate-setting application for its distribution business, the Board determined that it was not appropriate for the C factor to be applied to working capital:

***The OEB finds that the calculation of the capital factor will not include a component for working capital in rate base. The capital factor provides funding for capital expenditures not funded through the  $(I - X)$  adjustment, and the OEB has determined that providing additional funding for working capital is inappropriate in this context.<sup>51</sup>***

67. Despite this finding, HONI is proposing that the capital factor for the transmission side of the business apply to working capital amounts. While CME acknowledges that working capital makes up less of HONI's transmission capital amounts than it does for the distribution business,<sup>52</sup> HONI has failed to provide a principled reason why the C factor should apply to working capital amounts, or why there should be different treatment

<sup>50</sup> EB-2019-0082, Exhibit M1, Incentive Regulation for Hydro One Transmission, September 5, 2019, p. 44.

<sup>51</sup> EB-2017-0049, Decision and Order, March 7, 2019, p. 33.

<sup>52</sup> EB-2019-0082, Exhibit I, Tab 04, Schedule 2, part b).

between the distribution and transmission arms of its business. Accordingly, to the extent that Board approves a C factor, it should not apply to the working capital portion.

### 3.3 HONI's Productivity Savings

68. HONI has placed great emphasis on its productivity efforts in previous years, as well as throughout the plan term. According to HONI's evidence, they have committed to \$370 million dollars in productivity savings over the course of the application term.<sup>53</sup>
69. The productivity savings have been split into "defined" productivity savings for capital and OM&A, as well as "undefined" and "progressive" productivity savings as set out in the following chart:<sup>54</sup>

1 **Table 2: Productivity Savings Forecast Summary (\$Millions)**

<b>\$mm</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>	<b>Total</b>
Operations	47	52	53	53	54	259
Operations Progressive (Defined)	6	12	12	10	10	49
Corporate	12	11	9	7	6	45
<b>Capital Total</b>	<b>\$65</b>	<b>\$74</b>	<b>\$73</b>	<b>\$70</b>	<b>\$70</b>	<b>\$353</b>
Operations	9	10	9	9	9	45
Information Technology	6	9	10	10	10	44
Corporate	7	6	5	4	3	25
<b>OM&amp;A Total</b>	<b>\$22</b>	<b>\$25</b>	<b>\$23</b>	<b>\$23</b>	<b>\$22</b>	<b>\$114</b>
<b>Total Defined</b>	<b>\$87</b>	<b>\$99</b>	<b>\$97</b>	<b>\$93</b>	<b>\$92</b>	<b>\$468</b>
Operations Progressive (Undefined)	11	27	49	68	81	237
<b>Grand Total</b>	<b>\$98</b>	<b>\$126</b>	<b>\$146</b>	<b>\$161</b>	<b>\$173</b>	<b>\$704</b>
Progressive (Defined)	6	12	12	10	10	49
Progressive (Undefined)	11	27	49	68	81	237
Progressive Placeholder	17	39	61	78	91	286

70. According to HONI's evidence, progressive productivity savings are those that HONI will continue to implement over the plan term, but will provide the savings to ratepayers

<sup>53</sup> EB-2019-0082, Exhibit K1.1, Hydro One 2020-2022 Transmission Revenue Requirement Application Overview, October 21, 2019, p. 8

<sup>54</sup> EB-2019-0082, Exhibit A, Tab 3, Schedule 1, p. 21.

upfront. As a result, HONI's position is that it takes on the risk of completing those productivity initiatives successfully.

71. As an additional categorization of productivity, HONI also differentiates between tier 1 and tier 2 productivity. The former, according to HONI, are "hard savings" that are monitored cost reductions.<sup>55</sup> The latter are understood by HONI to be "good practices" such as avoided costs which don't necessarily reflect a lower cost to complete.<sup>56</sup>
72. As CME understands it, the table above only reflects the tier 1 productivity initiatives.
73. CME has several concerns with HONI's productivity proposal. In this regard:
- (a) The progressive productivity placeholder productivity benefits are entirely directed towards completing more work, rather than (at least partially) lowering proposed rate increases;
  - (b) To the extent that HONI fails to realize the promised productivity, their intention is to bring forward the higher-cost amounts in-service, thus increasing costs to ratepayers for the vast majority of the assets' life;
  - (c) Many of the productivity initiatives are not truly incremental; and
  - (d) HONI's proposed calculation of the productivity results cannot differentiate between true productivity and broader market conditions.
74. As a result of these concerns, CME submits that the true amount of productivity inherent in HONI's proposal, and the risk that HONI is taking is taking is lower than that posited in the application.

### **3.3.1 Productivity Benefits were Not Translated Into Lower Rates**

75. According to HONI's evidence, it now employs an eight-step planning process to determine what investments it wishes to fund during the plan term. The eight stages are set out as follows:

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<sup>55</sup> EB-2019-0082, Transcript, Vol. 3, p. 70, lines 2-27.

<sup>56</sup> EB-2019-0082, Transcript, Vol. 3, p. 70, lines 2-27.

The overall Investment Planning process is set out below in Figure 1.



**Figure 1 – Improved Eight-Step Investment Planning Process**

76. HONI's budget constraint is set out as part of the first step, the "investment planning context" phase.<sup>57</sup> After that phase, the candidate investments are scored, and during the "initial prioritization" phase, the budgetary constraint is layered onto the project investments to determine which projects are within budget, and which are not.<sup>58</sup>
77. As the planning process progresses, initiatives are added and dropped. The overall forecast number of investments and spend trended downward until the "Develop Final Plan" and "Review and Approval" stage(s) as indicated by the following chart:

**Table 1: Capital Spending Forecast (Millions)**

Category	Investment Planning Process Stage			
	Candidate Investment Development	Prioritization and Optimization	Enterprise Engagement	Develop Final Plan/Review and Approval
System Access	87	85	63	65
System Renewal	6,326	4,989	4,992	5,512
System Service	727	1,027	1,018	883
General Plant	476	439	439	447
Progressive Productivity Placeholder	N/A	N/A	N/A	(286)
Directive Adjustment <sup>1</sup>	N/A	N/A	N/A	(2)
<b>Total</b>	<b>7,616</b>	<b>6,540</b>	<b>6,511</b>	<b>6,619</b>

78. At that point, planned investments increased by \$394 million.<sup>59</sup> It is also at that point that HONI added its progressive productivity placeholder amount, and directive adjustment to

<sup>57</sup> EB-2019-0082, Transcript, Vol. 1, p. 48 line 25 to p. 49 line 8.

<sup>58</sup> EB-2019-0082, Transcript, Vol. 1, p. 49 line 9 to p. 50 line 6.

<sup>59</sup> EB-2019-0082, Transcript, Vol. 1, p. 56 lines 3-26.

the investment plan. The addition of these elements led to a net investment increase of \$108 million.

79. On cross-examination, HONI was asked whether or not the progressive productivity placeholder amount had been used exclusively to include more work within the existing budgetary constraints, or whether it had been used to lower the requested revenue required. HONI's answer was unequivocally that it used the productivity it found exclusively to do more work:

***MR. RUBENSTEIN: So you had a decision to make, I guess, Hydro One. You have determined that there's \$286 million in productivity, defined and undefined, that are in your plan. You can do more work for that \$286 million, or you could essentially lower the ask by 286 million. But you have determined that you would do more work. Do I take that?***

***MR. JESUS: As you can see from your exhibit SEC 28, there's close to 7.6 billion dollars' worth of risk that we need to -- projects that we need to carry out, and the prioritization landed on the 6.6 billion. So, yes, we are taking rates into account and we're landing on 6.6 billion because there's a lot of work, a lot of risk that is out on the system.***

***So the reality is that the productivity is being leveraged to deliver more work. [emphasis added]***<sup>60</sup>

80. CME submits that this is an inappropriate use of HONI's productivity. Ratepayers have consistently commented on the fact that cost is one of their top priorities. Even though HONI's customer engagement survey failed to capture its importance to ratepayers (see section 4.1.2 for further discussion), ratepayers have, on numerous occasions, cited costs as their overriding concern.
81. In this context, CME submits that a reduction of \$286 million to HONI's capital envelope is appropriate in order to give ratepayers the benefit of HONI's identified productivity savings.

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<sup>60</sup> EB-2019-0082, Transcript, Vol. 1, p. 59 line 14 – p. 60 line 2.

### 3.3.2 HONI's Risk is Restricted to the Three Year Plan Term

82. In a number of places in both their pre-filed evidence,<sup>61</sup> as well as their *viva voce* evidence,<sup>62</sup> HONI has stressed the risk that it is taking with respect to its up-front productivity.
83. CME does not agree that HONI is taking a significant risk. While HONI does bear some risk in relation to amounts that they would be unable to collect during the plan term as the result of higher than forecast costs, HONI confirmed that it would seek to in-service the full costs of any capital expenditures, regardless of whether they were not able to achieve the forecast productivity savings.<sup>63</sup> This would allow HONI to earn a return on these higher amounts for the balance of the assets' lives (60+ years).
84. Accordingly, the risk to HONI is much smaller than it has contended in its evidence.

### 3.3.3 Many Initiatives are Not Truly Incremental

85. While HONI has calculated that they will save \$370 million dollars as the result of productivity initiatives, in many cases, these calculations derive their baseline from as early as 2015. In other words, HONI may be more productive as the result of initiatives compared to their 2015 costs, but their actual incremental productivity from now through the custom IR plan period is much lower, and in some cases, non-existent. For instance, the savings from a number of initiatives are static throughout the plan term. These initiatives and their respective savings from 2019-2022 are shown below:<sup>64</sup>

Initiative Grouping	2019 Savings	2020 Savings	2021 Savings	2022 Savings
Transmission and Stations	\$0.7	\$0.7	\$0.7	\$0.7
Overtime Reductions	\$0.5	\$0.5	\$0.5	\$0.5
Scheduling Tool	\$0.9	\$0.9	\$0.9	\$0.9

<sup>61</sup> For instance, see Exhibit A, Tab 2, Schedule 3, p. 3 of 3.

<sup>62</sup> For instance, see EB-2019-0082, Transcript, Vol. 1, p. 17, lines 4-12; EB-2019-0082, Transcript, Vol. 1, p. 81, lines 15-25.

<sup>63</sup> EB-2019-0082, Transcript, Vol. 6, p. 81, line 12 – p. 82, line 9.

<sup>64</sup> EB-2019-0082, Exhibit JT2.28, Attachment 1.

<b>Initiative Grouping</b>	<b>2019 Savings</b>	<b>2020 Savings</b>	<b>2021 Savings</b>	<b>2022 Savings</b>
Wrench Time	\$0.5	\$0.5	\$0.5	\$0.5
Engineering	\$0.6	\$0.6	\$0.6	\$0.6
Transmission and Stations (OM&A)	\$1.2	\$1.2	\$1.2	\$1.2
Network Operating Efficiencies	\$1.0	\$1.0	\$1.0	\$1.0
Overtime Reductions (OM&A)	\$0.5	\$0.5	\$0.5	\$0.5
Wrench Time (OM&A)	\$2.3	\$2.3	\$2.3	\$2.3
Operations (CCC)	\$2.3	\$2.3	\$2.3	\$2.3

86. While these initiatives show static productivity impacts, and offer no incremental productivity during the plan term, HONI is calculating them at their face value (relative to the pre-initiative cost). In some cases, these initiatives began as early as 2015.
87. Similarly, HONI's productivity savings calculations for larger initiatives also overstate their impact by including existing savings amounts. For instance, the "procurement" initiative in undertaking JT2.28 shows productivity savings in 2020-2022 of \$30.3, \$34.9 and \$35.8 million respectively.<sup>65</sup> However, this initiative already yielded savings of \$27.9 in 2018 and \$25.1 in 2019. Accordingly, the true incremental productivity savings is approximately \$5-\$10 million per year, not \$30-\$35 million.
88. Some of HONI's productivity initiatives are regressing. For instance, corporate productivity initiatives, which saved HONI \$20.1 million in 2019, is forecast to decline every year, and only save \$13.6 million in 2022.<sup>66</sup> Despite the regression, HONI still counts these as productivity savings at their face value (e.g. \$13.6 million 2022). In this instance, HONI's productivity will be declining, but it will still claim to be finding productivity savings.

<sup>65</sup> EB-2019-0082, Exhibit JT2.28, Attachment 1.

<sup>66</sup> EB-2019-0082, Exhibit JT2.28, Attachment 1.



89. CME submits that the actual incremental productivity amounts that HONI committed to, and is taking the risk of achieving, are significantly lower than the amounts calculated in its evidence. Accordingly, CME submits that this militates in favour of the supplemental productivity espoused by CME in section 3.2.1. The supplementary stretch factor is a concrete and easy to administer method of ensuring that HONI endeavours to find productivity during the custom IR term.

**3.3.4 HONI's Productivity Calculations Do Not Differentiate Productivity from Market Conditions**

90. CME is also concerned that HONI's productivity calculations do not take into account market conditions or prices when determining the actual impact of the initiatives. For instance, a number of initiatives, such as procurement, involve activities on HONI's part that reduce the cost of purchasing. Activities include bundled purchasing or purchasing less expensive versions of products that have all of the required functionality. In CME's view, those would be appropriately categorized as productivity.
91. However, simply measuring the new unit cost in comparison with a historical unit cost will also capture broader market conditions. To the extent that those market conditions reduce the cost of an asset compared to its previous cost (this is especially true for technology purchases, such as computers), the reduction in cost will be counted by HONI's methodology as productivity, despite the fact that HONI has not done anything to become more productive.<sup>67</sup>

**3.4 Earnings Sharing Mechanism**

92. HONI has proposed an earnings-sharing mechanism that would provide ratepayers with 50% of any over-earnings over a 100 basis point dead-band above the allowed return on

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<sup>67</sup> EB-2019-0082, Transcript, Vol. 6, p. 96 lines 19-24.

equity.<sup>68</sup> The sharing would be asymmetrical in that if HONI fails to achieve its allowed return on equity there would be no impact on ratepayers.

93. This is the same mechanism as the one that the Board approved in HONI Distribution's proceeding bearing file number EB-2017-0049.<sup>69</sup>

94. Accordingly, CME supports the inclusion of the earnings sharing mechanism as proposed.

### **3.5 Z Factors and Off-Ramps**

95. HONI has requested a Z Factor mechanism be available for the term of their custom IR application. HONI proposes a \$3 million threshold for the Z Factor,<sup>70</sup> which is consistent with the Board's guidance set out in the *Filing Requirements for Electricity Transmission Applications*.<sup>71</sup>

96. CME supports the availability of a Z Factor mechanism for HONI, but submits that the Z Factor should be symmetrical. As stated in the Board's decision in EB-2017-0049:

***There is nothing to prevent the OEB from imposing Z-factor treatment for an unforeseen event that materially reduces costs and meets all of the Z-factor criteria, should one be identified.***<sup>72</sup>

97. The application of a symmetrical Z Factor for material increases and decreases in costs would align treatment of ratepayers with the treatment of the utility. Just as the utility should not be required to bear material and unforeseen increases in costs, the utility should not be allowed to benefit from material and unforeseen windfalls.

## **4.0 TRANSMISSION SYSTEM PLAN**

98. The transmission system plan ("TSP") is a document consisting of both an asset management plan, as well as regional planning considerations.<sup>73</sup> The TSP contains

<sup>68</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, p. 9 of 13.

<sup>69</sup> EB-2017-0049, Decision and Order, March 7, 2019, p. 40.

<sup>70</sup> EB-2019-0082, Exhibit I, Tab 05, Schedule 7, CME Interrogatory #7.

<sup>71</sup> Ontario Energy Board, *Filing Requirements for Electricity Transmission Applications*, Chapter 2: Revenue Requirement Applications, February 11, 2016, ss. 2.2.1 and 2.8.12.

<sup>72</sup> EB-2017-0049, Decision and Order, March 7, 2019, p. 43.

<sup>73</sup> Ontario Energy Board, *Filing Requirements for Electricity Transmission Applications*, Chapter 2: Revenue Requirement Applications, s. 2.4, p. 13.

information regarding the transmitter's strategic plans, as well as information on how investments are prioritized and selected, how the plan reflects the needs and preferences of the transmitter's customers, as well as how the utility plans to manage its assets during the plan period.

99. In its application, HONI is proposing a significant increase in its capital expenditures as part of its TSP. HONI's Historical and proposed capital spending are summarized in the below chart (\$Millions):<sup>74</sup>

2015	2016	2017	2018	2019	2020	2021	2022
\$899.4	\$866.3	\$950.0	\$1,000.0	\$1,038.2	\$1,191.2	\$1,317.7	\$1,369.6

100. Accordingly, the average capital spending is set to rise 31% in 2020-2022 as compared to 2017-2019.<sup>75</sup>
101. The vast majority of the increase in capital spending is driven by HONI's increases to the "system renewal" spending, which under HONI's proposal, will nearly double from an actual spend of \$689 million in 2015 to a planned spend of \$1,194 in 2022.<sup>76</sup>
102. HONI's witnesses indicated that this significant increase in spending was necessary due to "address the needs of the system" and "the needs of the customers".<sup>77</sup>
103. CME disagrees that HONI's proposal is adequately tailored to either consideration.
104. HONI's customer engagement had a number of methodological shortcomings, including its choice of respondents. As a result, the conclusions arrived at by HONI regarding customer's needs and preferences do not accurately reflect their concerns.
105. HONI's failure to meaningfully engage with end-use customers, who bear the vast majority of HONI's costs, caused HONI to undervalue the importance of cost to consumers, and

<sup>74</sup> SEC Compendium #1, Exhibit K1.2, pp. 2-3. Values populated for the years 2015-2018 are actuals, 2019 is the forecast value, and 2020-2022 are planned values. Values are denoted in millions of dollars.

<sup>75</sup> EB-2019-0082, Transcript, Vol. 1, p. 38, lines 8-22.

<sup>76</sup> SEC Compendium #1, Exhibit K1.2, p. 4.

<sup>77</sup> EB-2019-0082, Transcript, Vol. 1, p. 39, line 26 – p. 40, line 4.

led to a capital spending proposal that it is out of step with end-user's needs and preferences.

106. Furthermore, HONI's asset evidence does not demonstrate that a 31% increase in capital spending is warranted. HONI's asset condition assessments are still worryingly incomplete or erroneous in certain areas, and when more complete information is available, it shows that the condition of HONI's assets is stable, and does not justify HONI's significant spending increases.
107. Accordingly, CME submits that the Board should disallow capital expenditure amounts as described below.

#### **4.1 Customer Engagement Process**

108. CME is not satisfied with HONI's customer engagement process and, in particular, states that the Innovative Research Group Report (the "**IRG Report**") is not an accurate reflection of customer needs and preferences.

##### **4.1.1 Customer Engagement Process Still Does Not Include End Users**

109. Board Staff and intervenors raised concerns regarding HONI's customer engagement process during the EB-2016-0160 hearing.
110. These concerns were discussed and repeated during a meeting with stakeholders referred to by HONI at the "Transmission Customer Engagement Stakeholder Session" on March 29, 2017.<sup>78</sup>
111. Two themes which emerged from the Stakeholder Session was the need to engage with end users and the importance of HONI waiting for the Board decision in EB-2016-0160 prior to commencing customer engagement.<sup>79</sup>
112. HONI did not wait to receive direction from the Board on its prior Customer Engagement process before launching into its Customer Engagement for this Application.

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<sup>78</sup> CME Compendium, Panel #3, Exhibit K6.5, p. 18.

<sup>79</sup> CME Compendium, Panel #3, Exhibit K6.5, pp. 19-25.

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113. HONI's Customer Engagement process and retainer with Innovative Research Group began in the spring of 2017 and concluded with a final report by July 2, 2017, taking only a few months including preliminary planning sessions.<sup>80</sup>
114. The survey was completed in just over one month between May 11 and June 15, 2017.<sup>81</sup>
115. The Board released its decision in EB-2016-0160 on September 28, 2017 and revised decision on October 11, 2017.
116. In EB-2016-0160, the Customer Engagement was described by the Board as "adequate" but provided guidance to HONI on ways to improve the process, including that HONI "should have discussions with LDCs to determine practical ways to seek some input from their end users to inform HONI's application."<sup>82</sup>
117. The IRG Report does very little to engage with end users of LDCs – whose customers are expected by HONI to account for 92% of the rates revenue requirement (compared to 7% from transmission connected end-use customers and 1% from generators).<sup>83</sup>
118. HONI states that it attempted to obtain feedback from end users in the IRG Report by asking LDC's to "please respond to the questions in this survey with your customers in mind. Your feedback should be made with consideration to your customers' needs."<sup>84</sup> However, only 11 of 28 (40%) of LDC respondents provided survey responses that were informed by their own customer engagement activities or customer research.<sup>85</sup>
119. HONI also consulted with LDCs to obtain ideas as to how to solicit feedback from LDC end-users in the future, although none of those strategies were implemented or any survey data from those strategies put forward in support of HONI's application.<sup>86</sup>

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<sup>80</sup> CME Compendium, Panel #3, Exhibit K6.5, p. 16.

<sup>81</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, Section 1.3, Attachment 1 ("Innovative Research Group Report"), p. 3.

<sup>82</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, p. 24.

<sup>83</sup> EB-2019-0082, Exhibit I, Tab 7, Schedule 12, part a); CME Compendium, Panel #3, Exhibit K6.5, p. 122; EB-2019-0082, Transcript, Vol. 6, pp. 147-148.

<sup>84</sup> CME Compendium, Panel #3, Exhibit K6.5, p. 82.

<sup>85</sup> CME Compendium, Panel #3, Exhibit K6.5, p. 67.

<sup>86</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.3, p. 29.

120. Accordingly, CME does not accept that the efforts made by HONI to consult with end users were adequate in this application.
121. CME also does not accept that it would be overly difficult for HONI to conduct adequate consultation with end users. When asked about consulting with commercial and industrial customers, for example, HONI acknowledge at the hearing that it has contact information for these customers and that consultation with them is possible for the next Application:

***Mr. Gill ..... With respect to C and I customers attendance at our large customer conference, part of the work that I was doing throughout 2017 and 2018 was consolidating what we call a large customer group. So we have expanded that down to large distribution accounts. So there are..***

***Ms. Durant: So you have their contact information. You can get in touch with those groups?***

***Mr. Gill: So the folks who have a demand of 2 megawatts and above now have an assigned account executive to them. So that's an additional hundred accounts there. The company is in the process right now of expanding that model to a lower threshold.....***

***Ms. Durant: So it would be possible to engage with them in a more detailed level and to document their concerns in a survey like this one?***

***Mr. Gill: It terms of the next engagement that is being planned, there will most certainly be an opportunity to meet with this particular customer segment, either in dedicated interviews or at a forum, yes.***

122. It is CME's position that HONI could have done that level of consultation with the C&I customers in this Application.

#### **4.1.2 Other Engagement beyond the IRG Report Suggest that Rates Are the Most Important Priority**

123. It is well-established that HONI ratepayers are concerned about the cost of electricity.
124. In fact, that underlying assumption was built into the development of the IRG Report, as was explained by Mr. Lyle at the hearing:

***Mr. Lyle: If I can add one thing? In our initial discussions in planning this, and it is noted in the report that a number of pieces of prior information were brought to bear. One of those, for instance, is the Canadian Electricity Association survey which looks at customers all across Ontario and the rest of Canada.***

***It doesn't specifically deal with transmission issues, but issues like concern about price were well established in the discussion and known as we went forward. So there wasn't - - there wasn't any doubt by anyone developing the engagement that residential low volume customers were concerned about price.***

***Ms. Durant: And that wasn't what you were getting at when doing your survey, because it is known at Hydro One that most people care about price.***

***Mr. Lyle: Right, and I think it is in the actual document that has been filed.***

125. HONI references in its evidence unspecified customer surveys conducted by other LDCs which indicate that residential customers, small business customers and mid-market customers consider price to be their number one priority and reliability their number two priority while larger demand key accounts prioritize reliability over price.<sup>87</sup>
126. In HONI's Distribution Customer Engagement Report, keeping rates as low as possible was the number one customer priority for almost every customer segment (37% of residential/seasonal customers, 38% for small businesses, 36% for first nations, 46% for commercial and industrial customers and 41% for large distribution accounts).<sup>88</sup>
127. LDCs were the only customer group in HONI's Distribution Customer Engagement which did not prioritize keeping rates as low as possible as their number one priority – presumably because they can pass on increased rates to their customers.
128. HONI's application does not focus on keeping rates as low as possible and the IRG Report does not specifically ask the customers surveyed about rates. Many of the customers who participated in the survey identify the lack of questions about rates as a missed outcome.<sup>89</sup>
129. The only outcome listed as an option for HONI customers to rank in order of importance that came close to "rates" was productivity.<sup>90</sup>

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<sup>87</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.3, p. 29.

<sup>88</sup> EB-2019-0082, SEC Compendium Panel 3, Exhibit K6.4, pp. 45-50.

<sup>89</sup> For example, see EB-2019-0082, CME Compendium, Panel #3, Exhibit K6.5, pp. 42-45.

<sup>90</sup> EB-2019-0082, CME Compendium, Panel #3, Exhibit K6.5, p. 41.

130. Although HONI focuses in its evidence on various consultations beyond the IRG Report, it is only the IRG Report that is summarized in HONI's report to their Board of Directors leading up to the filing of this Application – and only the top five outputs of safety, reliability, outage restoration, power quality and customer service.<sup>91</sup>

#### **4.1.3 The Reliability Risk Model Remains Unreliable**

131. The Board in EB-2016-0160 also rejected the use of the Reliability Risk Model (the “RRM”) as a means of conveying to customers information about the value of capital investments in terms of system reliability, stating that further refinement and testing is needed.<sup>92</sup>
132. Nonetheless, HONI has used the same RRM in this Application.<sup>93</sup> The RRM is utilized in the IRG Survey as a means to quantify and communicate the outcomes associated with various investment scenarios.<sup>94</sup>
133. HONI acknowledges in its evidence the concerns raised by the Board in EB-2016-0160 that the model requires further refinement and testing if it is to be used to convey to customers information about the value of capital investments in terms of system reliability.<sup>95</sup>
134. Further, HONI has, since the last application, obtained a third party assessment by METSCO Energy Solutions Inc. (“METSCO”) which “led to similar conclusion and recommendations” regarding the RRM.<sup>96</sup> In particular, HONI states that:

**Metsco reviewed the Reliability Risk Model (“RRM”) and found that the analytical underpinnings and functionalities of the RRM trail advanced industry system reliability practices were used in asset management. In making this observation, Metsco found that a number of utilities do not nor have not until recently attempted to formally forecast system reliability in a comprehensive manner and suggests the RRM reflects continuous improvement in this area. However, as Hydro One uses the RRM as a customer communications tool to convey directional changes to reliability risk levels across spend scenarios, Metsco is of the view that the**

<sup>91</sup> EB-2019-0082, Exhibit I, Tab 7, Schedule 2, Attachment 1, p. 7; EB-2019-0082, CME Compendium Panel 3, Exhibit K6.4, p. 126.

<sup>92</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, pp. 21-24.

<sup>93</sup> EB-2019-0082, Transcript, Vol. 1, pp. 68-69.

<sup>94</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.3, Attachment 4, p. 1.

<sup>95</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.3, Attachment 4, p. 1.

<sup>96</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.3, Attachment 4, p. 1.



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***observed gaps pose no meaningful risks from an asset planning perspective. Hydro One must remain clear about the tool's purpose and the implications of its analysis.***<sup>97</sup>

135. This is not how the RRM is described to individuals who took the IRG survey where it is described as “a forward looking or leading indicator of system reliability performance”, “an outcome measure used to indicate the potential improvement or decline in system reliability as the result of an investment plan”, and that “this measure also serves as a directional indicator to inform the appropriate level of pacing of sustainment investments to avoid future decline in reliability.”<sup>98</sup>
136. Any reservations that HONI, the Board or METSCO had regarding the RRM were not communicated to survey participants.
137. The RRM is baked into the investment scenario survey questions and provides specific information to survey participants regarding a percentage increase or decrease in risk based on the four investment scenarios which were put forward which ranged from an increase in risk of approximately 30% for Scenario A (limited investment) to a decrease in risk of 15% for Scenario D (increase beyond the current level of investment).<sup>99</sup>
138. HONI relies on the fact that the EB-2016-0160 decision was released after its customer engagement process with IRG was complete as an explanation as to why the RRM was utilized again in this proceeding.<sup>100</sup> CME is not satisfied with this explanation.
139. The Board's decision in EB-2016-0160 was released on September 28, 2017. This Application was not filed until March 21, 2019 – nearly one year and six months later. The IRG customer engagement process took only a couple of months and culminated in a report dated July 2, 2017. It could have been repeated to address the directions and concerns raised by the Board.

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<sup>97</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.4, p. 7.

<sup>98</sup> EB-2019-0082, CME Compendium, Panel #3, Exhibit K6.5, p. 112.

<sup>99</sup> EB-2019-0082, CME Compendium, Panel #3, Exhibit K6.5, p. 101.

<sup>100</sup> EB-2019-0082, Transcript, Vol. 1, p. 69.

140. Further, the stakeholders who attended the “Transmission Customer Engagement Stakeholder Session” on March 29, 2017, discussed above, expressly warned HONI against embarking on a customer engagement process prior to obtaining the Board’s decision. In particular, the notes from the session provide that:

***5. Hydro One should wait for the OEB decision before talking to customers again.***

- ***This will assist in defining parameters and scenario building.***
- ***Results from Board decision will provide direction that may point you in a different direction.***

***6. “I’m not sure how you can go to your customers until the decision is known.”<sup>101</sup>***

141. Failing to wait for the Board’s decision in EB-2016-0160, and failing to conduct further formal customer engagement following release of the decision, was a fatal flaw in HONI’s customer engagement in this application, one which stakeholders expressly warned HONI about in the March, 2017 Stakeholder Session referred to above. It also shows that HONI failed to engage with feedback received from the Board itself when developing its investment plan options.
142. Based on shortcomings with the customer engagement process and concerns regarding the RRM, the OEB did not place significant weight on the evidence associated with these elements and did not “rely on the outcome as reported by Hydro One as compelling evidence of customer support for the proposed level of capital expenditures.”<sup>102</sup>
143. We ask that the Board do the same in this Application.

#### **4.2 Data Quality and Completeness**

144. CME remains concerned with the data quality and completeness that goes into HONI’s asset analytics system, and is ultimately expressed through HONI’s investment prioritization.

<sup>101</sup> EB-2019-0082, CME Compendium, Panel #3, Exhibit K6.5, p. 20.

<sup>102</sup> EB-2019-0082, Transcript, Vol. 6, pp. 183-184.

145. In this proceeding, HONI provided a copy of its Internal Audit Report on its Investment Planning Support Tools, dated October 31, 2017. In this report, HONI's internal auditors found that the asset analytics data quality remained poor.<sup>103</sup> The audit report described the risk in the following terms:

***Poor quality data from source systems that are used as inputs to the Asset Analytics (AA) tool has resulted in unreliable Asset Risk Index calculations/outputs from the tool...***

***Analysis of these (data quality) measures for stations and lines asset composite ARI show that stations have low data completeness while lines have low confidence levels...***

***Almost 10% of Supporting Factors for distribution stations are either missing or using default values while 12% of Supporting Factors for Transmission Stations are either missing or using default values.***<sup>104</sup>

146. HONI also retained METSCO to opine on HONI's assets analytics system. METSCO found that HONI had the following data availability for transformers:

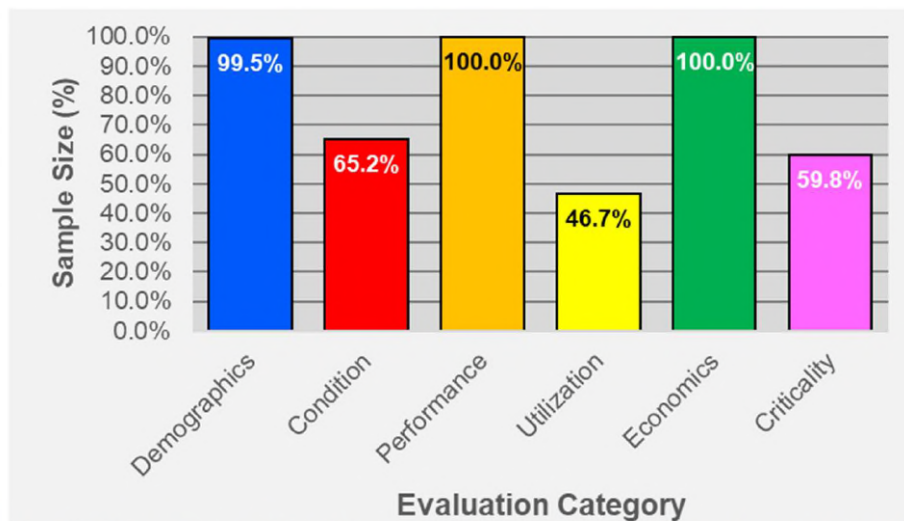


Figure 6. Station Power Transformer Average Sample Sizes for each Evaluation Category

147. In their report, METSCO stated that it considered HONI's condition data (65.2% complete) to be "robust"; however, CME has two concerns with this pronouncement.

<sup>103</sup> EB-2019-0082, CME Compendium, Panel #1, Exhibit 2.1, p. 55.

<sup>104</sup> EB-2019-0082, Exhibit JT 1.10, Attachment 2, p. 7 of 11.

148. First, METSCO's reasoning does not engage with HONI's broader data availability and quality. METSCO stated that it found HONI's condition data to be robust because HONI's condition score is a singular metric that is solely concerned with asset degradation, as opposed to most utilities, where the condition score is an overall health index that show condition, demographics and utilization information.<sup>105</sup>
149. CME notes however that HONI has even less utilization data (46.7%) for its transformers than it does condition data (65.2%).<sup>106</sup> Since HONI lacks significant quantities of both condition and utilization data, CME submits that the compound unavailability of asset data will cause as many suboptimal investment decisions as missing data in a single composite measure will.
150. Furthermore, CME does not believe that METSCO was aware of the widespread instances of incorrect data that plague HONI's transformer condition data.<sup>107</sup> In a related report filed by HONI in this proceeding, EPRI determined that nearly 20% of HONI's transformer asset condition assessments did not match those conducted by EPRI.<sup>108</sup> According to the filed evidence, issues with HONI's data were the cause of the incorrect transformer asset condition assessments.
151. In response to an interrogatory posed by CME, HONI clarified that there were two separate data issues: first, data that HONI collected or entered into the system incorrectly;<sup>109</sup> second, data that HONI extracted from the wrong area or component, which accordingly does not accurately reflect the condition of the asset.<sup>110</sup>
152. Troublingly, HONI's response to this widespread problem has been anemic. HONI initiated a project to test automation of the transformer test results. HONI hopes that this automation will eliminate the clerical errors that come from manual entries. This project is

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<sup>105</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.4, Attachment 13, p. 40 of 106.

<sup>106</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.4, Attachment 13, p. 40 of 106.

<sup>107</sup> EB-2019-0082, Transcript, Vol. 2, p. 35, line 9 – p. 37, line 6.

<sup>108</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 1.4, p. 8.

<sup>109</sup> EB-2019-0082, Exhibit I, Tab 05, Schedule 13.

<sup>110</sup> EB-2019-0082, Exhibit I, Tab 05, Schedule 13.

not anticipated to be completed until the end of 2019, and accordingly was not complete when the investment decisions in this plan were determined.<sup>111</sup>

153. Regarding instances where asset information is taken from the wrong asset component(s), HONI has not proposed to do anything differently. During the technical conference, HONI confirmed that as a result of not changing their approach, the percentage of incorrect readings that result from taking samples from the wrong transformer components will continue unabated,<sup>112</sup> and will continue to be problematic for HONI's asset condition data. This data directly feeds into HONI's investment decision making.
154. HONI has also confirmed that the data quality issues discovered by EPRI do not overlap with instances where there is no condition data.<sup>113</sup> Accordingly, while HONI stated in its evidence that it possesses 65.2% of transformer condition data, CME submits that the amount of accurate data that HONI possesses for transformer conditions is actually significantly lower.
155. As a result, CME submits that the Board should apply a reduction to HONI's capital spending proposal in recognition of the fact that assets that are planned to be replaced may not require such investment, due to incomplete or incorrect information in HONI's asset analytics system.

#### **4.3 System Renewal Spending**

156. The major driver behind HONI's significant increase in capital expenditures is spending on system renewal investments. The asset condition of HONI's major asset classes; however, do not support such a drastic spending increase, both at the macro-level as well as with respect to specific capital investments.

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<sup>111</sup> EB-2019-0082, Exhibit I, Tab 05, Schedule 13.

<sup>112</sup> EB-2019-0082, Technical Conference Transcript, August 12, 2019, p. 42, line 15 – p. 43, line 28.

<sup>113</sup> EB-2019-0082, Exhibit I, Tab 05, Schedule 13.

157. The overall condition assessment for HONI's major asset categories in this application as well as from HONI's most recent previous transmission application (EB-2016-0160) are provided in the following table:<sup>114</sup>

Asset Category	% Assets at High or Very High Risk (EB-2016-0160)	% Assets at High or Very High Risk (EB-2019-0082)
Transformers	15%	17%
Circuit Breakers	11%	9%
Protection Systems	27%	27%
Conductors (km)	9%	13%
Wood Poles	12%	13%
Underground Cables (km)	14%	3%

158. The asset condition assessments show a mix of asset trends. Most major asset categories have a generally stable condition trend over time, with some having modest increases to the percentage of assets in high-risk condition (transformers and wood poles), and some showing modest to significant decreases (circuit breakers and underground cables).
159. Accordingly, CME submits that the evidence of HONI's full complement of assets does not demonstrate a need for an increase in investment at all, much less a nearly 50% increase to system renewal spending during the plan term.<sup>115</sup>

#### **4.3.1 Conductors**

160. One of the major drivers of HONI's significant increase in capital spending over the course of the plan period is its proposed conductor replacements. According to HONI's evidence, it has spent \$156.5 million on conductor replacement over the three-year period from 2016 to 2018.<sup>116</sup> In contrast, HONI is proposing to ramp-up conductor spending to \$553.9 million in the upcoming three-year period from 2020 to 2022.<sup>117</sup> HONI is therefore proposing to

<sup>114</sup> EB-2019-0082, Exhibit JT 1.21.

<sup>115</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 3.1, p. 3.

<sup>116</sup> EB-2019-0082, Exhibit JT1.24, Attachment 1. Derived from 2016, 2017 and 2018 listed actuals for the conductor portfolio of \$68, \$36.5 and \$52 million respectively.

<sup>117</sup> EB-2019-0082, Exhibit JT1.24, Attachment 1. Derived from 2020, 2021 and 2022 forecast amounts for the conductor portfolio of \$150.8, \$191.4 and \$211.7 million respectively.

spend three and a half times more money on conductor replacement in the upcoming terms than they did during the previous three-year term.

161. In its pre-filed evidence, HONI seemed to indicate that the reason for this increase was two fold: one was the increase in the number of assets that were found to be at “high-risk” condition as part of HONI’s asset assessment; and second was the prospective number of assets that were aging past HONI’s estimated service life or “**ESL**” for conductors.<sup>118</sup> On cross-examination however, HONI’s witnesses clarified that the sole driver for the increased level of investment was the increase in the number of assets that were assessed as being in high-risk condition.<sup>119</sup>
162. HONI’s pre-filed evidence indicated that the proportion of high-risk conductors had increased from 9% to 13% as confirmed by testing relative to the EB-2016-0160.<sup>120</sup>
163. The cause of the increase in high-risk level conductors was the increase in conductor testing that occurred since EB-2016-0160.<sup>121</sup> Since EB-2016-0160, HONI reduced the backlog of unassessed conductor assets by approximately 10%.<sup>122</sup> As a result of this testing, some assets, whose condition was not previously known, were moved to the high-risk category. This re-categorization of newly assessed assets increased the proportion of high-risk conductors from 9% to 13%.<sup>123</sup>
164. While HONI’s increased testing has increased the number of conductors in high-risk condition, this does not represent a degradation of HONI’s assets, and will not lead to a greater number of outages than what has been experienced by HONI in the past.
165. During cross-examination, HONI’s witnesses clarified that outages from conductors are a function of both the conductors that are in high-risk condition, whose condition is known to HONI, as well as conductors that are in high-risk condition, whose condition is unknown

<sup>118</sup> EB-2019-0082, Exhibit B, TSP Section 2.2, p. 57 of 117; EB-2019-0082, Exhibit B, TSP Section 3.1, p. 16 of 24.

<sup>119</sup> EB-2019-0082, Transcript, Vol. 2, p. 10, line 10 – p. 11, line 2.

<sup>120</sup> EB-2019-00082, Exhibit B, TSP Section 2.2, p. 56.

<sup>121</sup> EB-2019-0082, Exhibit B, TSP Section 2.2, p. 56; EB-2019-0082, Transcript, Vol. 2, p. 10, line 10 – p. 11, line 2.

<sup>122</sup> EB-2019-00082, Exhibit B, TSP Section 2.2, p. 56.

<sup>123</sup> EB-2019-00082, Exhibit B, TSP Section 2.2, p. 56; EB-2019-0082, Transcript, Vol. 2, p. 12, line 21 – p. 13, line 13.

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to HONI and that are categorized in the “needs assessment” category.<sup>124</sup> In other words, outages happen as a result of assets in both the “high-risk” and “needs assessments” categories of assets.

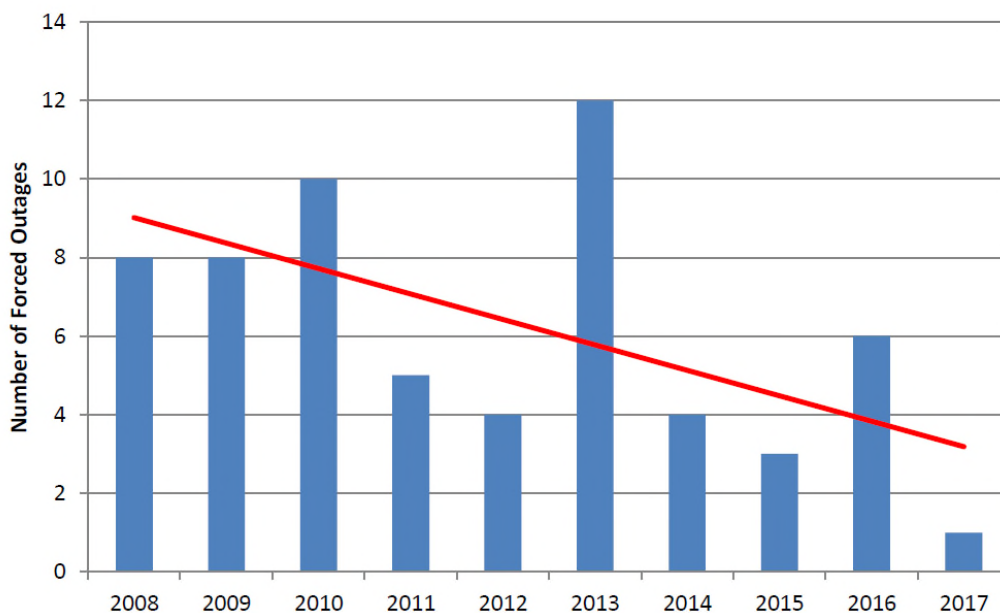
166. Accordingly, the increase in the number of high-risk conductors from 9% to 13%, brought about by measuring more conductors in the “needs assessment” category, will not impact reliability going forward. The actual condition and function of the assets has not degraded. HONI has simply re-categorized them. Since outages were already a result of high-risk assets in both categories, the fact that those assets have switched between the “needs assessment” category and the “high-risk” category will not increase outages.
167. If anything, an increase in the number of conductors that are assessed would mean a slight decrease in conductor related outages, as HONI would be able to better prioritize replacements even among the high-risk conductor population.
168. The evidence regarding the conductor caused outage trend is consistent with this view. Set out below are the conductor related frequency and duration statistics for the years 2008-2017:<sup>125</sup>

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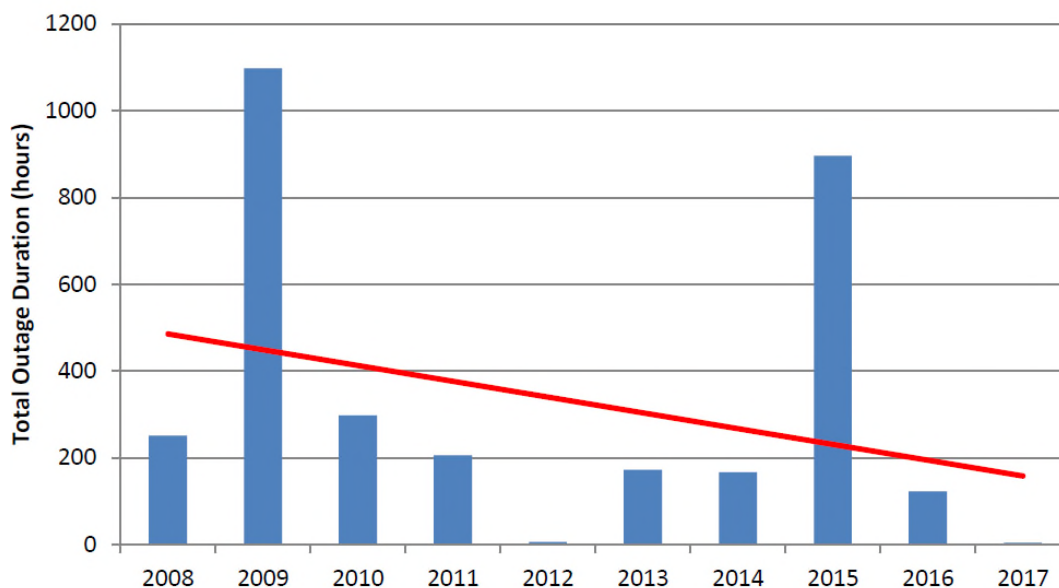
<sup>124</sup> EB-2019-0082, Transcript, Vol. 2, p. 12, lines 9-20.

<sup>125</sup> EB-2019-0082, Exhibit B, TSP Section 2.2, p. 58.





**Figure 19 - Overhead Conductor Forced Outage Frequency**



**Figure 20 - Overhead Conductor Forced Outage Duration**

169. As demonstrated by Figure 19 and 20 from HONI's pre-filed evidence, on average the overhead conductor forced outage frequency and duration are both trending downwards over time.

170. The estimated service life of HONI's conductors fleet also does not indicate a need for a significant increase in conductor investments either.
171. Previously, HONI had assigned an ESL of 70 years to conductors. Using this as a guide, HONI estimated that approximately 19% of their conductor fleet was operating beyond its ESL in EB-2016-0160.<sup>126</sup>
172. HONI's ESL for conductors, however, has proven to be too conservative. In a report conducted by EPRI, it was recommended that HONI increase the ESL of conductors to 90 years, to reflect how resilient and long-lived HONI's conductor fleet actually is.<sup>127</sup> As a result, in HONI's evidence in the current proceeding, HONI estimates that only 5% of the conductor fleet is at or beyond its ESL.<sup>128</sup> Even if no replacements are made throughout the entire plan period, the number of conductors operating at or below their ESL would still be significantly below what HONI determined it was in EB-2016-0160.
173. Accordingly, CME submits that HONI's proposal to increase spending on its conductor fleet dramatically is not supported by the evidence, nor justified under the circumstances. Given that the asset condition is not truly degrading over time, the outage statistics are improving over time, and the number of assets reaching their ESL is less than that outlined by HONI in EB-2016-0160, CME believes that the Board should reduce HONI's proposed planned capital expenditures on conductors to be in line with historical levels.

#### **4.3.2 Oil Circuit Breakers**

174. As part of HONI's TSP, HONI intends to replace 247 oil circuit breakers. Of the 247 circuit breakers scheduled for replacement, HONI has measured 69 of them to have above acceptable levels of PCBs.<sup>129</sup> Accordingly, 178 of the oil circuit breakers scheduled for replacements are not contaminated with unacceptable levels of PCBs.<sup>130</sup> HONI's

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<sup>126</sup> EB-2019-0082, CME Compendium #1, Exhibit K2.1, p. 14.

<sup>127</sup> EB-2019-0082, Exhibit B1, Tab 1, Schedule 1, TSP Section 3.2, p. 18.

<sup>128</sup> EB-2019-0082, CME Compendium #1, Exhibit K2.1, p. 3.

<sup>129</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 3.2, p. 14 of 28.

<sup>130</sup> EB-2019-0082, CME Compendium #1, Exhibit K2.1, p. 38. EB-2019-0082, Transcript, Vol. 2, p. 27 lines 8-15.

justification for the replacements of the non-PCB contaminated circuit breakers include, *inter alia*, that oil circuit breakers have unacceptable reliability/availability, and have excessive cost impacts.<sup>131</sup>

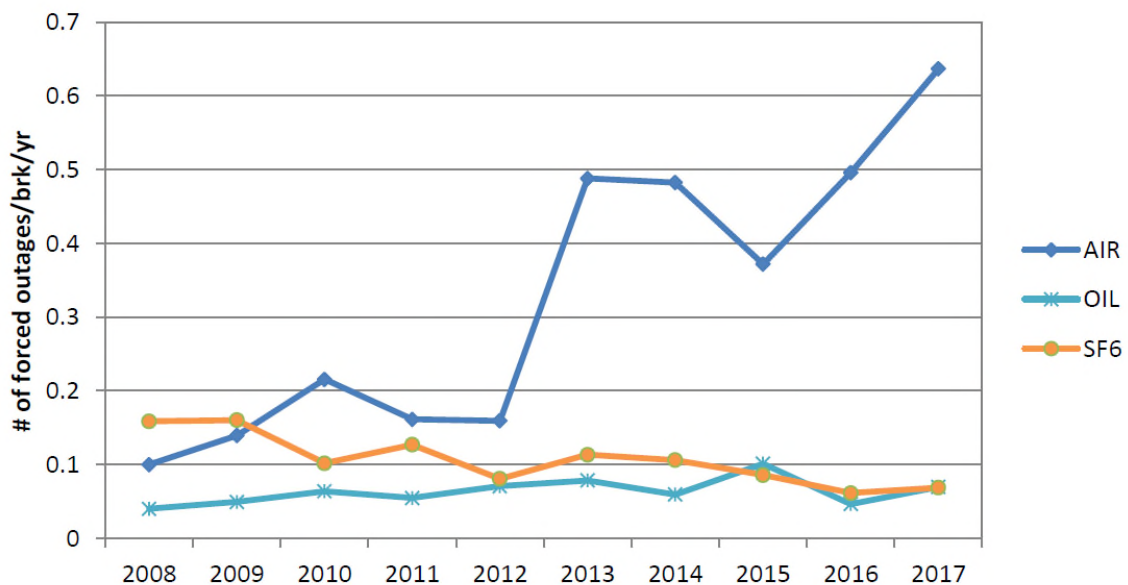
175. CME supports the replacement of the circuit breakers that have been determined to have excessive levels of PCBs. CME submits, however, that HONI's proposed pacing for replacement of the remaining oil circuit breakers is not justified by the evidence in this proceeding.
176. HONI filed a report by EPRI that surveyed transmitters to determine whether oil circuit breakers were more costly or difficult in terms of maintenance and repair than single pressure gas breakers (the "**OCB Report**"). Single pressure gas breakers would replace the oil circuit breakers.
177. The OCB Report determined that there would likely be marginal benefits to HONI from replacing oil circuit breakers with single pressure gas breakers. In this regard, the OCB report found:<sup>132</sup>
  - (a) A slim majority of respondents (3 of 5) found single pressure gas breakers to be more reliable than oil circuit breakers, while 2 of 5 respondents found the replacement breakers to either be equivalent in terms of reliability, or less reliable.
  - (b) Two thirds of the OCB Report respondents found that it would cost them the same amount of money, or less, to perform minor maintenance on existing oil circuit breakers than it would on HONI's proposed replacement breakers.
  - (c) Two thirds of the OCB Report respondents also found that it would cost the same amount of money to perform major maintenance on oil circuit breakers than it would on HONI's proposed replacements.

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<sup>131</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 3.2, p. 16 of 28.

<sup>132</sup> EB-2019-0082, CME Compendium #1, Exhibit K2.1, p. 40.

178. Furthermore, HONI's outage statistics do not show a need for a surge in oil circuit breaker replacements. While circuit breaker caused outage duration and frequency are trending upwards, the evidence shows that these outages are driven by air-blast circuit breakers, not oil circuit breakers. For instance, the chart below provides outage frequency by circuit breaker type:<sup>133</sup>



**Figure 11 - Summary of Forced Outages by Breaker Type**

179. As shown above, oil circuit breakers have had a stable impact on the number of forced outages for the past decade.
180. Accordingly, CME submits that the replacement of oil circuit breakers with single pressure gas breakers will not have a significant impact on breaker reliability or on the cost of maintenance of the breaker fleet.
181. With respect to HONI's ability to maintain a reserve of interoperable spare parts, CME submits that a less torrid pace of replacement would provide spare parts to ameliorate HONI's concern. HONI's evidence is clear that oil circuit breakers can be salvaged for

<sup>133</sup> EB-2019-0082, Exhibit B, TSP Section 2.2, p. 20 of 117.

parts to support the remaining fleet.<sup>134</sup> Accordingly, the replacement of the oil circuit breakers for PCB concerns, in addition to a more modest pace of replacement for non-PCB oil circuit breakers, should provide sufficient spare parts for HONI's replacement pool.

#### **4.3.3 Escalating Project Capital Spending**

182. CME is concerned that HONI's cost estimation for air-blast circuit breaker projects categorically under-estimates the required costs. As a consequence, the Board is being asked to approve a capital spending envelope that does not accurately portray the true costs of the work HONI is proposing.
183. For instance, the following table shows the forecast project cost of replacing air blast circuit breakers that was provided during HONI's previous transmission application (EB-2016-0160) compared to their current total forecast costs:<sup>135</sup>

<b>Project</b>	<b>Estimated Cost (EB-2016-0160) [Millions]</b>	<b>Estimated Cost (EB-2019-0082) [Millions]</b>	<b>Variance [Millions]</b>
Beck #1 SS	\$24.1	\$30.7	\$6.6
Beck #2 TS	\$90.7	\$110.2	\$19.5
Bruce A TS	\$104.9	\$111.2	\$6.3
Bruce B SS	\$65.2	\$85.5	\$20.3
Cherrywood TS 230 KV	\$60.6	\$88.9	\$28.3
Lennox TS	\$83.7	\$88.1	\$4.4
Richview TS	\$95.5	\$94.9	(\$0.6)
<b>Total</b>	<b>\$524.7</b>	<b>\$609.5</b>	<b>\$84.8</b>

<sup>134</sup> EB-2019-0082, Exhibit B, Tab 1, Schedule 1, TSP Section 3.2, p. 14 of 28.

<sup>135</sup> EB-2019-0082, SEC Compendium for Panel #1, Exhibit K1.2, pp. 66-82.

184. As demonstrated above, HONI's cost estimates have, with one exception, gone up between EB-2016-0160 and now. In total, HONI estimates that these seven air-blast circuit breaker projects will cost a total of \$84.8 million more than they estimated in EB-2016-0160, an average increase of 16%.
185. To compound the issue, HONI now proposes to add an additional five circuit breaker projects.

#### **4.4 OPEB Capitalization Policy**

186. In March of 2017, the Financial Accounting Standards Board ("**FASB**") published the Accounting Standard Updated No. 2017-07 ("**ASU 2017-07**"). ASU 2017-07 changed USGAAP accounting treatment for certain OPEB components.<sup>136</sup> Specifically, it prohibited the capitalization of the interest cost, return on plan assets and amortization of actuarial gains/losses and prior service costs.
187. Since ASU 2017-07 was published after HONI's previous revenue requirement proceeding, the Board approved a deferral account, effective January 1, 2018, which was to record the OPEB costs previously capitalized that had been prohibited by ASU 2017-07.<sup>137</sup> The Board also found that it would be appropriate to determine whether HONI should be able to continue capitalizing OPEBs despite ASU 2017-07 in its next revenue requirement proceeding.<sup>138</sup>
188. In its application, HONI has proposed two alternative approaches to accounting for these amounts. First, HONI proposes to continue capitalizing these amounts, despite ASU 2017-07.<sup>139</sup> In the alternative, HONI proposes to continue to use the deferral account created in EB-2017-0338 to account for the outstanding OPEB components.<sup>140</sup>

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<sup>136</sup> Financial Accounting Standards Board, *Accounting Standards Update No. 2017-07, Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, March 10, 2017, [https://fasb.org/jsp/FASB/FASBContent\\_C/CompletedProjectPage&cid=1176168898401](https://fasb.org/jsp/FASB/FASBContent_C/CompletedProjectPage&cid=1176168898401) [accessed December 15, 2019].

<sup>137</sup> EB-2017-0338, Decision and Order, May 10, 2018, p. 4.

<sup>138</sup> EB-2017-0338, Decision and Order, May 10, 2018, p. 4.

<sup>139</sup> EB-2019-0082, Exhibit H, Tab 1, Schedule 2, p. 10.

<sup>140</sup> EB-2019-0082, Exhibit H, Tab 1, Schedule 2, p. 10.

189. In their submissions, OEB Staff did not support the continued capitalization of OPEB costs that were prohibited by ASU 2017-07. As CME understands it, they do so on the following bases:<sup>141</sup>

- (a) No other utility that follows USGAAP has requested OEB approval to continue capitalizing costs prohibited by ASU 2017-07;
- (b) Over the long-term, capitalization of the OPEB amounts will be more expensive for ratepayers, due to the return on rate base;
- (c) This would exacerbate the Board's concern regarding HONI's generous capitalization policy, as set out in its EB-2016-0160 decision; and
- (d) HONI's alternative approach increases regulatory burden without commensurate additional benefit.

190. CME agrees with Board Staff's submissions, and agrees with the Board's statement from EB-2016-0160, wherein the Board stated:

***That said, the OEB shares the concerns of those who question the continued appropriateness of the large capitalization amounts that USGAAP allows compared to the amounts allowed under MIFRS regulatory accounting purposes.***<sup>142</sup>

191. Accordingly, CME submits that the Board should reject HONI's proposed approaches to the OPEB amounts impacted by ASU 2017-07.

## **5.0 OPERATIONS MAINTENANCE & ADMINISTRATION COSTS**

### **5.1 Employee Compensation**

192. CME continues to have concerns regarding the quantum of HONI's compensation costs.

193. It is CME's position that there should be a reduction to HONI's compensation costs to the extent that HONI remains above market median. Further, CME submits that additional reductions should be ordered to address three aspects of HONI's compensation: generous

<sup>141</sup> EB-2019-0082, Ontario Energy Board Staff Submission, pp. 78-79.

<sup>142</sup> EB-2016-0160, Decision and Order, September 28, 2017, Revised October 11, 2017, p. 82.

incentive packages for managers that are tied to profits to HONI, increasing overtime pay which is not benchmarked and shareholder grants that are a benefit to HONI employees at no cost to the corporation. These reductions are addressed in turn below.

### **5.1.1 Reduction for Amount Above Market Median**

194. The Board has continuously commented on these compensation costs in recent decisions. Nonetheless, HONI has done little to move towards market median and expressed during the current hearing “the 50<sup>th</sup> percentile is not an appropriate place to compare Hydro One.”<sup>143</sup>

195. In EB-2013-0416 (distribution rate application), HONI produced a compensation benchmarking report by Mercer which demonstrated that compensation was 10% higher than the median of its comparator group. The Board commented that:

***HONI did not provide sufficient evidence in support of its proposed compensation spending. The company did not demonstrate that the market requires the level of compensation proposed in order to attract and retain the necessary employees. In the absence of such evidence the OEB will use the market median as a reference point for the percentage of compensation costs that will be included in the rates paid by HONI's Customers.***<sup>144</sup>

196. The Board disallowed half of the 10% premium over market median. In doing so, the Board recognized HONI's progress in “getting closer to market median” and directed that HONI file “a compensation study similar to the one filed in this proceeding so that the OEB can continue to benchmark HONI's compensation against that paid by comparable companies.”<sup>145</sup>

197. In EB-2016-0160, the Board was concerned about HONI's lack of progress towards market median and reduced HONI's compensation by \$15 million per year:

***The OEB is also concerned that HONI's progress towards bringing its total compensation levels down to the market median has now reversed. The Mercer Report indicates that a reduction in compensation amounts of about \$12.5 million is required to bring***

<sup>143</sup> EB-2019-0082, Transcript, Vol. 6, p. 59.

<sup>144</sup> EB-2013-0416/EB-2014-0247, Decision, March 12, 2015, p. 24.

<sup>145</sup> EB-2013-0416/EB-2014-0247, Decision, March 12, 2015, p. 25.



***compensation levels to that median. Moreover the OEB agrees that HONI's total compensation amounts are likely understated because not all items of HONI compensation were included therein.***

***After considering all of the evidence related to the amounts for compensation that HONI seeks to recover from transmission services ratepayers, the OEB finds that compensation amounts in the total OM&A envelopes for 2017 and 2018 of \$412.7 million and \$409.3 million are unreasonably high by an amount of approximately \$15.0 million in each year. These compensation envelope reduction amounts reflect the OEB's finding that HONI has failed to establish that the significantly increased levels of compensation for executives, directors and other managerial personnel should be recoverable from ratepayers.<sup>146</sup>***

198. The Board also considered incentive payments to employees in its reasons in EB-2016-0160. As in this case, the incentive payments, particularly the short-term incentive program, was available to management level employees. Submissions were made by OEB Staff and several intervenors regarding the significant magnitude of incentive payment amounts and their terms which were heavily weighted to prompt the delivery of value to shareholders.<sup>147</sup> The Board stated that it “shares the concerns of those parties who expressed the view that costs of incentive plans that are primarily designed to deliver value to the shareholder should not be recoverable from utility ratepayers.”<sup>148</sup> The Board found that the holding company should have greater responsibility for the compensation amounts that relate to its transformation and its commitments to increase shareholder value which are of little if any value to consumers of electricity transmission services.<sup>149</sup>
199. In the most recent review of HONI's compensation, the Board in EB-2017-0049 where the Board summarized as follows:

***The OEB finds that its ongoing concern about Hydro One's compensation costs being higher than comparable companies has not been satisfactorily addressed. This concern has been expressed in almost every OEB decision involving both the distribution and transmission costs of Hydro One for the last 10 years ...***

.....

<sup>146</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, p. 59.

<sup>147</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, p. 59.

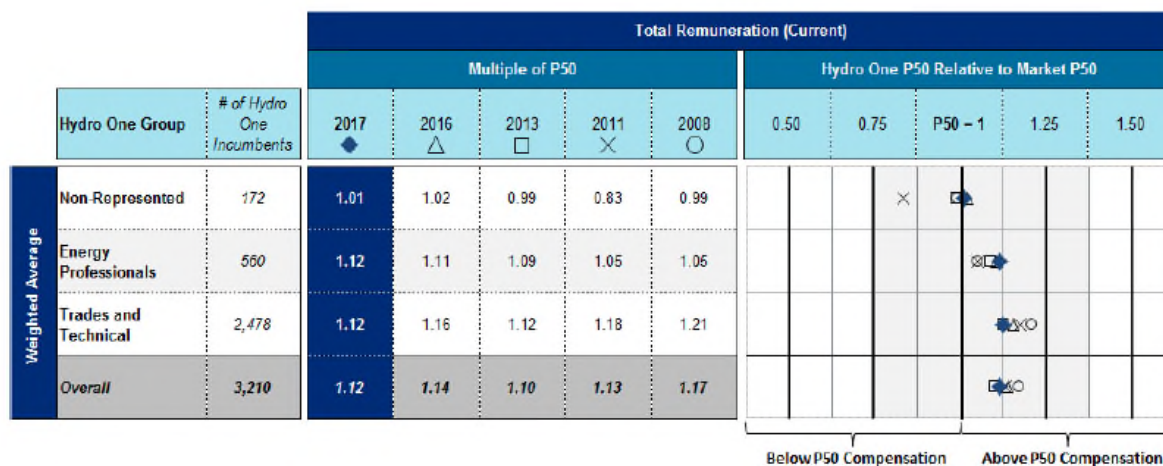
<sup>148</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, p. 57.

<sup>149</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, pp. 59-60.

*Although the OEB acknowledges that Hydro One attempted to make some progress in both the unionized and non-unionized compensation areas, its compensation levels remain significantly above the market median. The latest Mercer compensation study, filed by Hydro One on April 20, 2017, concluded that Hydro One is positioned approximately 12% above the market median. In previous years, Hydro One's position has ranged from 10% above median in 2013 to 14% in 2016.*

*While the OEB understands the limitations associated with the collective agreements, it does not believe that sufficient progress has been made by Hydro One in the last few years to bring its compensation levels closer to market median. In fact, one could argue that the benchmarking results are getting worse (10% above median in 2013, 12% above median in 2017).<sup>150</sup>*

200. The Mercer report considered in EB-2017-0049 is the same report which has been filed by HONI in this proceeding. The Mercer report is dated April 4, 2018 and considers 2017 compensation levels ("**2017 Mercer Report**").
201. The 2017 Mercer Report recalculated HONI's compensation at 12% above market median and shows the following history of HONI's compensation levels compared to market median. HONI is further from market median than it was in 2013.<sup>151</sup>



202. There is a slight improvement in HONI's position compared to market median between 2016 and 2017. However, the 2017 Mercer Report contains important limiting language

<sup>150</sup> EB-2017-0049, Decision and Order, March 7, 2019, p. 110.

<sup>151</sup> EB-2019-0082, Exhibit F, Tab 4, Schedule 1, Attachment 2, Mercer "Compensation Cost Benchmarking Study Hydro One Networks Inc.," 04 April 2018, p. 5 of 34.

as a result of altered comparator companies and benchmark jobs. The 2017 Mercer Report expanded the comparator employers to include organizations from which HONI contract employees (i.e. private companies).<sup>152</sup> As a result of the altered comparator groups, the 2017 Mercer Report states that “While these changes may have an impact on the study-over-study comparison, Mercer believes they better reflect the current workforce and balance of jobs at HONI.”<sup>153</sup>

203. CME submits that movement towards market median from 2016 to 2017 is marginal and that the changes may have resulted entirely as a result of the altered comparator groups and jobs benchmarked. In any event, HONI's positioning, when compared to market median, continues to trend away from market median.
204. HONI provided an estimate of the value amount above market median allocated to its transmission business and the market median used in the Mercer study. The dollar amount above market median ranged from over \$34 million in 2019 to over \$39 million in 2022.<sup>154</sup>

**Response:**

- a) An estimate of the dollar difference between the weighted average total compensation for Hydro One's employees allocated to its transmission business and the market median used in the study is as follows:

	Study Year	2020	2021	2022
<b>Estimated Dollar Difference</b> (Hydro One to Market Median)	\$34,485,965	\$38,566,291	\$40,010,087	\$39,079,490

205. HONI acknowledges in its evidence, and on cross-examination, that while employee compensation is contained in the OM&A portion of their evidence, the biggest impact with

<sup>152</sup> EB-2019-0082, Exhibit F, Tab 4, Schedule 1, Attachment 2, Mercer “Compensation Cost Benchmarking Study Hydro One Networks Inc.,” 04 April 2018, p. 3 of 34.

<sup>153</sup> Mercer “Compensation Cost Benchmarking Study Hydro One Networks Inc.,” 04 April 2018 at p. 4.

<sup>154</sup> EB-2019-0082, Exhibit I, Tab 7, Schedule 55, part a).

respect to how it collects its compensation amounts is in the capital portion of rates at approximately 75%.<sup>155</sup>

Transmission Compensation Breakdown between Capital and OM&A	2014	2015	2016	2017	2018	2019	2020	2021	2022
% Capital	65.8%	66.1%	72.6%	63.8%	69.6%	72.2%	73.8%	76.0%	76.3%
% OM&A	34.2%	33.9%	27.4%	36.2%	30.4%	27.8%	26.2%	24.0%	23.7%
% Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

206. In past decisions, the Board has granted an annual reduction for employee compensation with reference to the amount at which HONI is above market median. HONI has attempted to reduce the amount of that reduction by off-setting various reductions related to OM&A as set out in SEC 55.<sup>156</sup> According to HONI, the amount above market median allocated to OM&A in 2020 is \$10.1 with the rest (approximately \$38,466,291) allocated to Capital.
207. HONI then suggests a number of inappropriate and irrelevant adjustments to the “above market median” figure. These amounts are summarized in the below chart and reduce the amount above market median for the OM&A portion of the compensation costs to only \$500,000 in 2020.<sup>157</sup>

Net Mercer Median Reductions Allocated to OM&A (\$M)	2020
Mercer Median - Tx OM&A	10.1
Pension Reduction OM&A	(5.5)
OPEB Reduction OM&A	(2.4)
Executive Comp. Reduction	(1.5)
The Directive	(0.1)
Total Net Mercer OM&A Reductions	0.5

208. It is CME’s position that these adjustments are not proper as they do not have an impact on the “above market median” calculation made by Mercer.
209. For example, Mr. Morris noted under cross-examination that “there are aspects of these categories that would not affect Hydro One’s relative position to market”. He pointed to

<sup>155</sup> EB-2019-0082, Transcript, Vol. 6, p. 55.

<sup>156</sup> EB-2019-0082, CME Compendium, Panel 2, Exhibit K5.2, pp. 68-69.

<sup>157</sup> EB-2019-0082, Exhibit I, Tab 7, Schedule 55, p. 2 of 3.

executive compensation, as an example, as it could be driven by executives who were not covered by the Mercer Study. He also raised a concern regarding the pension reduction. Mr. Jodoin clarified that what HONI was attempting to do with this cart is identify “specific revenue requirement reductions we made to our application. Granted, Hydro One wouldn’t be able to speak to the relative peer group used in the study and what would change. So absolutely no, we are not trying to reforecast what Mercer has done. We’re simply trying to identify compensation-related reductions we’ve made relative to the study point.”<sup>158</sup>

210. The challenges with removing the above-noted reductions from the Mercer calculations are dealt with in more detail in SEC’s submissions, which CME agrees with.
211. It is CME’s position that there should be a reduction for the full amount that HONI remains above-market median for compensation given the significant attention this issue has drawn over the last several applications and the limited improvement that HONI has demonstrated to date.
212. CME also supports Staff’s submission that HONI should be required to file a plan as to how it will move its compensation numbers towards market median going forward. The evidence at the hearing suggested that HONI took the position that achieving market median is not possible and there is a sense that HONI is not working diligently towards this goal.

#### **5.1.2 Overtime Expenses are not benchmarked and are rising significantly**

213. The Mercer Report does not benchmark for overtime.<sup>159</sup> The calculation and reduction sought above regarding the amount that HONI is above market median for compensation costs would not include any consideration of overtime pay.
214. The amount of overtime pay provided to the Society of United Professionals (the “**Society**”), the Power Workers’ Union (“**PWU**”) and temporary employees and allocated

<sup>158</sup> EB-2019-0082, Transcript, Vol. 6, pp. 60-61.

<sup>159</sup> EB-2019-0082, Transcript, Vol. 6, pp. 47-49.

to transmission has increased significantly since 2017 and remains high throughout the 2020-2022 period.

215. Questions were asked during the hearing regarding the increasing overtime spend, including by the Board.
216. One factor contributing to the increase in overtime spend was the latest round of bargaining with the PWU which resulted in a decrease in hour threshold required to be worked prior to triggering overtime pay at a rate of 2x the employee's standard pay.<sup>160</sup>
217. Other factors noted at the oral hearing was the increase in storms and the "significant increases in our overall work program."<sup>161</sup>
218. HONI is paying overtime and budgeting for overtime at a growing and significant rate.
219. Total transmission allocated overtime pay/projected overtime pay increased from a total of \$22,311,906 in 2016 to a projected \$66,410,085 in 2022 – an increase of almost 200% in six years. The increases are across all employee groups entitled to overtime as outlined below:

- (a) Society: from \$1,792,765 in 2016 to \$5,717,210 in 2022
- (b) PWU: from \$15,656,038 in 2016 to \$47,243,112 in 2022
- (c) Temporary: from \$4,863,103 in 2016 to \$13,549,763 in 2022

Transmission Society Represented	2014	2015	2016	2017	2018	2019	2020	2021	2022
Base Pay	67,393,687	66,909,144	65,179,365	72,517,488	70,250,107	83,210,524	91,575,087	96,245,302	95,123,535
Overtime	2,940,988	2,853,433	1,792,765	4,635,127	5,942,030	5,446,164	5,512,817	5,626,666	5,717,210
Lump Sums	-	-	618,063	1,312,146	-	-	-	-	-
Burdens	45,275,079	45,463,351	34,228,158	37,334,202	30,162,557	35,344,898	39,492,527	42,142,638	42,322,714
Share Grants	-	-	-	-	1,243,401	1,142,108	1,127,076	1,086,518	1,041,623
Transmission Society Represented Total	115,609,754	115,225,928	101,818,351	115,798,964	107,598,095	125,143,693	137,707,506	145,101,125	144,205,083

<sup>160</sup> EB-2019-0082, CME Compendium Panel 2, Exhibit K5.2, p. 63; EB-2019-0082, Transcript, Vol. 5, pp. 27, 35.

<sup>161</sup> EB-2019-0082, Transcript, Vol. 5, pp. 32-33.

Transmission PWU Represented	2014	2015	2016	2017	2018	2019	2020	2021	2022
Base Pay	148,298,536	146,298,728	145,538,184	158,933,735	154,996,772	165,116,892	185,433,184	196,453,689	196,258,552
Overtime	28,468,143	24,728,915	15,636,038	36,486,246	46,990,537	43,212,279	44,677,729	45,980,102	47,243,112
Lump Sums	-	1,345,306	2,637,844	-	-	-	-	-	-
Burdens	99,626,956	99,406,896	76,427,624	81,823,907	66,549,350	70,135,836	79,969,621	86,020,581	87,320,079
Share Grants	-	-	-	3,778,937	3,382,051	3,283,939	3,254,468	3,156,020	3,007,446
Transmission PWU Represented Total	276,393,635	271,779,845	240,239,691	281,022,825	271,918,710	281,748,947	313,335,001	331,610,392	333,829,189

Temporary Transmission	2014	2015	2016	2017	2018	2019	2020	2021	2022
Casual Trades	117,432,836	114,683,317	126,561,770	120,254,743	126,691,541	134,172,558	134,088,990	131,778,118	130,179,945
Unrepresented	1,037,380	1,062,954	1,429,735	659,976	839,280	223,899	248,376	261,054	259,128
Society Represented	2,184,967	2,099,278	1,820,954	1,537,491	1,117,826	562,536	580,988	477,407	472,698
PWU Represented	9,810,066	5,736,423	6,145,715	5,764,657	4,887,005	2,944,456	3,233,454	3,394,711	3,365,930
Overtime	10,311,405	8,102,478	4,863,103	10,950,269	18,688,912	13,415,649	13,206,444	13,486,554	13,549,763
Other Allowances	-	-	-	-	-	-	-	-	-
Burdens	8,939,318	8,507,504	9,066,085	8,652,709	9,331,999	9,361,693	9,492,662	9,436,827	9,413,095
Temporary Transmission Total	149,715,971	140,191,954	149,887,362	147,819,845	161,556,564	160,680,791	160,850,913	158,834,670	157,240,559

220. CME is concerned regarding the quantum of overtime paid to HONI employees and the high budgeted amounts for overtime in 2020-2022.

221. We do not have any evidence as to how HONI's overtime practices and policies compare to other organizations.

222. The evidence is that overtime is difficult to benchmark, however, Mr. Morris did elaborate that there are policy studies available that would provide a summary of overtime policies and the relative prevalence of various features in the market. Mr. Morris explained:

**Mr. Morris:** Yes. There are studies that look at overtime policy and that's, I think, what you are describing.

**Ms. Durant:** Yes.

**Mr. Morris:** So when does overtime kick in, in terms of number of hours, whether it is on hours worked in a day, hours worked in a week.

**Ms. Durant:** Ok.

**Mr. Morris:** And then what the actual amount of the overtime is.

**Ms. Durant:** And those overtime policy studies, would they be available to show, you know, what's common in the market, you know, where the market is going in terms of overtime? What would they actually show?

**Mr. Morris:** They would show typically a summary of policies and the relative prevalence of various features. What they tend not to show

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*is the amount of overtime worked, because it's more programmatic.*<sup>162</sup>

223. The amount of overtime paid by HONI has continued to increase without adequate explanation and without added value to ratepayers. HONI has not made efforts to review its overtime policies and practices to ensure that they align with the market or explain the dramatic increase in overtime spend.

### **5.1.3 STIP and LTIP Bonuses are Weighted Towards Profit to Shareholders**

224. Changes in compensation for the non-representative group are within HONI's control (rather than limited by collective bargaining agreements) and spending on this employee group has not been curtailed or adjusted downwards. In fact, HONI has "refreshed" the short term and long term incentive plans ("STIP" and "LTIP") since HONI became a public company, which has resulted in increased compensation to these managerial employees.<sup>163</sup>
225. The STIP in particular is directly contributing to HONI's above-market positioning as stated in the Mercer Report.<sup>164</sup>
226. The STIP and LTIP are described throughout Exhibit F, Tab 4, Schedule 1. Both are essentially bonus programs. To summarize, the STIP is designed to reward management for achievement of annual team and individual goals, align corporate goals and objectives with individual goals, focus on short-term goals and immediate priorities and "reward and retain top performers." The STIP rewards are based on HONI's performance, as measured against the team scorecard, discussed in detail below.<sup>165</sup>
227. The LTIP was introduced in 2016 for select senior leaders and is designed to reward executives for longer-term value creation and foster "alignment with shareholder

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<sup>162</sup> EB-2019-0082, Transcript, Vol. 5, p. 49.

<sup>163</sup> EB-2019-0082, Transcript, Vol. 5, p. 23.

<sup>164</sup> Mercer "Compensation Cost Benchmarking Study Hydro One Networks Inc.," 04 April 2018, p. 4; EB-2019-0082, CME Compendium Panel 2, Exhibit K5.2, p. 25.

<sup>165</sup> EB-2019-0082, Exhibit F, Tab 4, Schedule 1, p. 25.



interests”, support line-of-sight and achievement of near-term objectives that lead to long-term value creation, attract and retain top talent and align compensation with current market practices.<sup>166</sup>

228. HONI has historically had low levels of attrition at the management level. No studies were implemented prior to implementation of the STIP or LTIP which indicated that management-level turnover was a concern to the corporation.<sup>167</sup>
229. Short Term and Long Term Incentive payments for both the transmission and distribution non-represented managerial employees have increased significantly since HONI became a public company, as outlined below.<sup>168</sup>

Transmission Unrepresented	2014	2015	2016	2017	2018	2019	2020	2021	2022
Base Pay	33,396,323	34,508,999	33,641,927	38,772,661	36,544,290	38,524,614	43,137,614	45,511,365	45,048,884
Burdens	22,435,650	23,448,136	17,666,653	19,961,342	15,690,642	16,363,898	18,603,459	19,927,923	20,043,316
Other Allowances	3,452,267	2,367,920	3,296,601	3,983,397	5,723,344	3,596,819	4,021,881	4,237,275	4,194,217
STI	4,055,590	4,414,248	4,565,907	7,257,372	6,297,493	4,618,185	5,308,380	5,674,271	5,630,422
LTi	-	-	241,898	2,350,267	3,730,541	632,252	984,137	1,070,633	847,416
ESOP	-	-	774,963	886,803	540,602	1,771,039	1,963,382	2,046,258	1,998,514

Distribution Unrepresented	2014	2015	2016	2017	2018	2019	2020	2021	2022
Base Pay	37,601,338	39,909,527	41,751,062	42,861,848	46,685,158	53,165,528	50,517,625	50,137,653	52,495,756
Burdens	25,260,579	27,117,681	21,925,067	22,066,579	20,044,720	22,582,842	21,786,151	21,953,622	23,356,606
Other Allowances	3,886,951	2,738,490	4,091,222	4,403,509	7,119,612	4,963,755	4,709,947	4,668,000	4,887,548
STI	4,578,312	5,117,332	5,712,824	8,142,916	7,564,939	7,819,365	7,464,246	7,442,291	7,839,166
LTi	-	-	249,764	2,535,402	4,764,858	1,870,199	1,374,938	1,140,263	1,210,384
ESOP	-	-	708,363	811,624	677,410	2,290,696	2,128,505	2,075,874	2,153,951

230. A copy of the STIP Employee Guide is in the record and was reviewed with the witnesses on panel 2.<sup>169</sup> According to HONI, 96% of management employees received a STIP payment for the 2018 year (paid out in 2019). The average STIP payout was \$30,683 (median \$19,858).<sup>170</sup>
231. The amount of the STIP payment is based on a calculation which is found in the employee guide. The basic calculation is excerpted below. Essentially, each management employee has a “target bonus” which is based on a percentage of their salary and the amount of the

<sup>166</sup> EB-2019-0082, Exhibit F, Tab 4, Schedule 1, p. 25.

<sup>167</sup> EB-2019-0082, Exhibit I, Tab 5, Schedule 41.

<sup>168</sup> EB-2019-0082, Exhibit I, Tab 5, Schedule 43, Attachment 1.

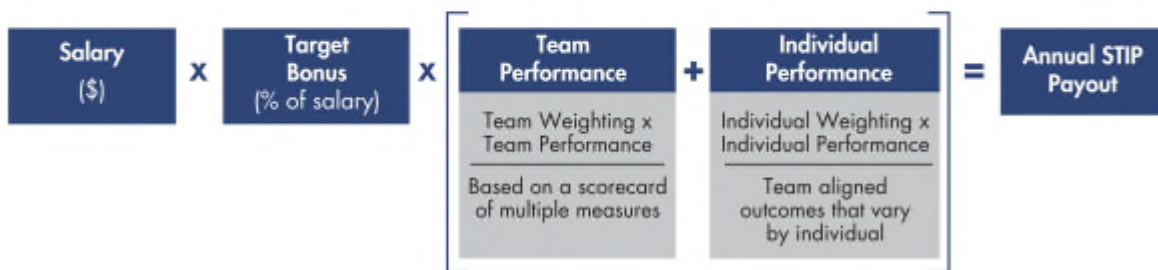
<sup>169</sup> EB-2019-0082, Exhibit I, Tab 5, Schedule 43, Attachment 1.

<sup>170</sup> EB-2019-0082, Exhibit I, Tab 5, Schedule 43.

target bonus can increase or decrease depending on team performance (from the Team Scorecard) and individual performance.<sup>171</sup>

### STIP OVERVIEW

Hydro One's STIP provides an annual incentive payout based on Individual and Team (corporate) performance, against pre-determined goals and measures. The STIP payout is calculated based on the following formula. Each of the elements of STIP calculation is described in more detail below.



232. The Team Scorecard is an important component of the incentive programs and is used to calculate the team performance metrics.<sup>172</sup>
233. The 2019 Team Scorecard is excerpted below. The single largest component of the Team Scorecard for 2019 is "Net Income". This was also the case in 2018. Net Income to shareholders is consistently given a weight of 30% of the Team Scorecard, higher than Health & Safety (10%), the Work Program (25%), Productivity Savings (10%) and Customer Service (25%):

<sup>171</sup> EB-2019-0082, Exhibit I, Tab 5, Schedule 43, Attachment 1, p.1.

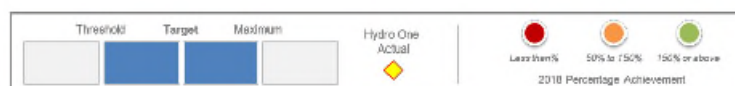
<sup>172</sup> EB-2019-0082, Exhibit F, Tab 4, Schedule 1, Attachment 4; EB-2019-0082, Transcript, Vol. 5, pp. 42-43.

2019 Team Scorecard							
Attachment 4 Page 1 of 1							
Corporate Goal	Component Weight	Definition	Measure	Sub-Component Weight	2019 Performance Levels		
					Threshold	Target	Maximum
<b>Health &amp; Safety *</b>	10%	Recordable Incidents	Incidents per 200,000 hours	100%	1.11	1.05	0.99
<b>Work Program</b>	25%	Transmissions (Tx) Reliability – Average duration of unplanned interruptions to multi-circuit (mc) supplied delivery points (SAIDI)	System Average Interruption Duration Index - mc (minutes)	25%	8.4	8.1	6.3
		Distribution (Dx) Reliability – Average duration of interruptions in hours that a customer can expect to experience (SAIDI)	System Average Interruption Duration Index (hours)	25%	7.0	6.3	6.0
		Tx In-Service Additions - Delivery Accuracy, ability to deliver to a budget	Variance (%) to approved budget of \$951M	25%	+/- 6%	+/- 4%	+/-1%
		Dx In-Service Additions - Delivery Accuracy, ability to deliver to a budget	Variance (%) to approved budget of \$556.5M	25%	- 5 % / + 4%	- 3% / + 2%	- 1% / + 1%
<b>Net Income</b>	30%	Net Income to Common Shareholders	\$M	100%	Redacted		
<b>Productivity</b>	10%	Savings in \$M	\$M	100%	\$164.1	\$193	\$222
<b>Customer</b>	25%	Residential & Small Business	Customer Satisfaction	40%	71%	77%	80%
		Transmission Connected & Local Distribution Companies (LDCs)	Customer Satisfaction	40%	85%	90%	92%
		Commercial and Industrial	Customer Satisfaction	20%	73%	77%	80%

234. The 2018 Team Scorecard results provide an interesting illustration on how these scoring metrics work in practice. In 2018, the Team Scorecard final results saw management benefit from a 166.91% score for the team portion of incentive payments, even while the organization achieved a 0% on the transmission reliability metric.
235. The total 2018 Team Scorecard result was inflated as a result of HONI exceeding its “net income to common shareholders” target of \$705.79 million by over \$100 million dollar (actuals noted to be \$806.67 million). By achieving a 200% score on net income to shareholders, that single metric accounted for 60% of the total Team Scorecard result. The full 2018 Team Scorecard is excerpted below:<sup>173</sup>

<sup>173</sup> EB-2019-0082, Exhibit I, Tab 12, Schedule 19, Attachment 1.

Component	Measure	Performance Levels and Actual Achievement ( ♦ represents Hydro One 2018 Achievement)	Weighting	Percentage Achievement	Contribution to Team Scorecard
<b>Health &amp; Safety</b>					
Recordable Incidents	Recordable Incidents per 200,000 hours	Threshold: 1.30 Target: 1.10 Max: 1.00 1.11	10.00%	93.85%	9.39%
<b>Work Program</b>					
Tx Reliability	Minutes per Delivery Point (SAIDI)	Threshold: 9.20 Target: 7.40 Max: 5.40 15.37	6.25%	0.00%	0.00%
Dx Reliability	Hours per Customer (SAIDI)	Threshold: 7.50 Target: 7.00 Max: 6.80 6.82	6.25%	190.00%	11.88%
Tx In Service Capital	Variance (%) to approved budget of \$1,174M	Threshold: +/-6.00% Target: +/-4.00% Max: +/-1.00% -1.16%	6.25%	194.65%	12.17%
Dx In Service Capital	Variance (%) to approved budget of \$641M	Threshold: +/-5.00% Target: +/-3.00% Max: +/-1.00% -4.23%	6.25%	83.99%	5.25%
<b>Financials</b>					
Net Income	Net Income to Common Shareholders - \$M	Threshold: 660.71 Target: 705.79 Max: 756.71 806.67	30.00%	200.00%	60.00%
<b>Productivity</b>					
Productivity Savings	Productivity Savings - \$M	Threshold: 103.10 Target: 114.50 Max: 140.00 115.51	10.00%	182.40%	18.24%
<b>Customer Service</b>					
Dx Satisfaction: Small & Residential Customers	Dx Customer Satisfaction (SMB & Res.)	Threshold: 73.00% Target: 73.00% Max: 76.00% 76.00%	12.50%	200.00%	25.00%
Tx Satisfaction: Large Customers	Tx Customer Satisfaction (Large Cust.)	Threshold: 84.00% Target: 86.00% Max: 90.00% 90.00%	12.50%	200.00%	25.00%
<b>Total</b>					<b>166.91%</b>



236. In the EB-2016-0160 decision, the Board shared concerns raised by intervenors that “costs of incentive plans that are primarily designed to deliver value to the shareholder should not be recoverable from utility ratepayers.”<sup>174</sup>
237. As demonstrated in the 2018 Team Scorecard result, managers of HONI are incentivized to generate income for shareholders and are rewarded in the form of general STIP and LTIP payments as a result.
238. Accordingly, it is CME's position that the STIP and LTIP are expensive programs that are contributing to HONI's above-market positioning and that it has limited benefit to ratepayers.

<sup>174</sup> EB-2016-0160, Decision and Order, Revised October 11, 2017, p. 56.

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## 6.0 DEFERRAL AND VARIANCE ACCOUNTS

239. As part of its application, HONI proposes to create, continue and dispose of outstanding amounts in a number of variance and deferral account. In this regard, CME wishes to make submissions on the following two accounts:

- (a) The In-Service-Capital Additions Variance Account; and
- (b) The OPEB Asymmetrical Carrying Charge Account.

### 6.1 In-Service-Capital Additions Variance Account

240. HONI proposes to continue the existing In-Service Capital Additions Variance Account. This account tracks the difference between the revenue requirement from actual in-service capital additions and the revenue requirement associated with the OEB-approved in-service capital additions.

241. To the extent that the amount of cumulative in-service additions are 98% or less than the OEB-approved in-service capital additions, the balance of the account would be negative and refunded to ratepayers.<sup>175</sup> The account, however, is asymmetrical, so cumulative in-service additions above the OEB approved level will not be recorded in the account.<sup>176</sup>

242. As part of calculating the values for the in-service-capital additions variance account, HONI proposes to exclude verifiable productivity savings.<sup>177</sup> These productivity gains refer to incremental productivity found during the plan term on top of those already included in the current revenue requirement.<sup>178</sup>

243. CME submits that the Board should reject this proposed modification. As stated earlier in these submissions, CME has a number of concerns with how HONI calculates its productivity results. Accordingly, it is not clear to CME how stakeholders can ensure that

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<sup>175</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, p. 10 of 13.

<sup>176</sup> EB-2019-0082, Exhibit A, Tab 4, Schedule 1, p. 10 of 13.

<sup>177</sup> EB-2019-0082, Argument in Chief of Hydro One Networks Inc., November 22, 2019, p. 119.

<sup>178</sup> EB-2019-0082, Ontario Energy Board Staff Submissions, December 11, 2019, p. 135.

the productivity amounts that HONI proposes to remove from the calculation of the account are truly the results of productivity.

## **6.2 OPEB Asymmetrical Carrying Charge Account**

244. In 2017, the Board issued the *Regulatory Treatment of Pension and Other Post-employment Benefits (PEBs) Costs* report.<sup>179</sup> In the report, the Board set out that rates for pension and OPEB costs would be set with reference to the accrual costs, rather than cash costs of these programs. The Board also directed utilities to set up a variance account to track the difference between accrual amounts collected from ratepayers and actual cash payments made, with a carrying charge applied to the differential.<sup>180</sup>
245. As part of the report, the OEB provided a default method of calculating the total gross accrual cost used in calculating the variance in this account.<sup>181</sup>
246. HONI also proposes an alternate methodology for the calculation of the OPEB Asymmetrical Carrying Charge Account. The report provides that a utility can suggest alternative calculation methodologies.
247. HONI has proposed an alternative method of calculating the forecast accrual amount in rates. HONI proposes to sum the following amounts to determine the total accrual cost as the sum of the following, less cash expenses:<sup>182</sup>
- (a) OPEB costs recorded in OM&A;
  - (b) The capitalized OPEB Expense recovered as part of the depreciation of PP&E;  
and
  - (c) The annual recovery of the OPEB costs recorded in the OPEB Cost Deferral Account and recovered over a 20 year period.

<sup>179</sup> EB-2015-0040, Report of the Ontario Energy Board, Regulatory Treatment of Pension and Other Post-employment Benefits (OPEBs) Costs, September 14, 2017.

<sup>180</sup> EB-2019-0082, Exhibit H, Tab 1, Schedule 2, p. 10.

<sup>181</sup> EB-2015-0040, Report of the Ontario Energy Board, Regulatory Treatment of Pension and Other Post-employment Benefits (OPEBs) Costs, September 14, 2017, p. 12.

<sup>182</sup> EB-2019-0082, Exhibit H, Tab 1, Schedule 2, p. 12.

248. As pointed out by Board Staff, HONI's alternate calculation proposal only records OPEB costs that have been capitalized to rate base from January 1, 2018 onwards.<sup>183</sup> It does not include amounts that were capitalized prior to that point. As a result, HONI's methodology minimizes the carrying charges owing to ratepayers.<sup>184</sup>
249. CME submits that the Board has determined an adequate methodology to calculate the carrying charges that occur as the result of HONI borrowing ratepayer funds to pay for future OPEB liabilities. The Board's methodology does not limit the application of carrying charges only to those amounts capitalized after January 1, 2018. Accordingly, the Board should reject HONI's proposal for an alternative calculation for the OPEB Asymmetrical Carrying Charge Account.

## 7.0 COSTS

250. CME requests that it be awarded 100% of its reasonably incurred costs in connection with this matter.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 16<sup>th</sup> day of December, 2019.



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Emma Blanchard  
Erin Durant  
Scott Pollock

Counsel for CME

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<sup>183</sup> EB-2019-0082, Ontario Energy Board Staff Submissions, December 11, 2019, p. 130.

<sup>184</sup> EB-2019-0082, Ontario Energy Board Staff Submissions, December 11, 2019, p. 130.