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Ontario Energy Board
2300 Yonge Street
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June 11, 2020
Our File: EB20190082

Attn: Christine Long, Registrar & Board Secretary

Dear Ms. Long:

Re: EB-2019-0082– Hydro One Tx 2020-2022 – Draft Rate Order Comments

We are counsel to the School Energy Coalition ("SEC"). Pursuant to the Board's Decision and Order ("Decision"), these are SEC's comments on Hydro One Networks Inc.'s ("Hydro One") Draft Rate Order ("DRO").

***In-Service Additions (System Access, System Service, and General Plant)*.** In addition to translating the capital expenditure reductions mandated by the Board's decision into in-service additions, Hydro One had also adjusted the in-service additions to account for changes in the timing of certain projects.[1] Hydro One references these adjustments in its explanation for the calculation of the System Access, System Service, and General Plant in-service additions.

SEC has several concerns with Hydro One's adjustments related to changes in the timing of capital work projects.

The DRO is meant to implement the Board's Decision, it is not for further refinements and updates to Hydro One's capital plan. This is especially important considering the Board's approval is based on a forecast capital envelope and not specific projects. If the Board determines that adjustment for more recent information on timing of certain projects is appropriate, SEC is concerned that no information has been provided in the DRO related to the reasons for the change in timing, their appropriateness, and how the changes have been calculated.

SEC is specifically concerned that while Hydro One may have moved originally forecast 2019 projects into 2020, it has not made the necessary corresponding adjustment to the 2019 closing rate base. For example, Hydro One notes that for General Plant, the overall in-service addition variance from its application was only $0.6M over the 2020-2022 rate period, even though the in-service adjustment based on the Board's disallowance of $4.3M.[2] The difference was attributable to what it calls "project

[1] Draft Rate Order ["DRO"], p.19
[2] DRO, p.19

timing", which SEC believes is a reference to projects supposed to be in-service pre-2020, but are now expected to be in-service during this rate plan.[3]

If the Board allows these adjustments to the test period in-service additions for timing, then a corresponding adjustment to the closing 2019/opening 2020 rate base will need to be made, as those projects were not in-service as originally forecast at the beginning of the year. If these adjustments are not made, then Hydro One will be double counting the projects by treating the same capital as in-service when the rate period begins, and then adding them again to rate base during the rate period. Similar adjustments would also have to be made for movements of projects within the 2020 to 2022 rate period.

It is not clear from the DRO and its schedules if Hydro One has made all these necessary adjustments. Hydro One may have already done so, but because of the way it presents the rate base calculation in DRO exhibits[4] (i.e., it only provides the average utility plant and not the opening and closing numbers as would normally be required in the Board's Appendix 2-BA) there is no way to determine whether it has, and if so, correctly. If it has not, Hydro One must make these adjustments. If it has, Hydro One should provide the details, including the supporting calculations, in its reply submissions. Regardless, Hydro One should provide detailed opening and closing annual rate base numbers and a full explanation of the adjustments made.

In-Service Additions (System Renewal) SEC is confused by how Hydro One has implemented the Board's System Renewal capital expenditure reduction. Hydro One's DRO calculation includes a $59.3M increase in 2020 in System Renewal in-service additions[5], even though it has allocated a $55.1M reduction in the 2020 System Renewal capital expenditures.[6]

Hydro One's explanation is that there is a much lower capital expenditure to in-service addition ratio for transmission, as compared to distribution, because of the relative size and length of the capital work. It says that this results in the allocated $55.1M reduction in capital expenditures in 2020 which will equal an amount less than that on an in-service addition basis. SEC understands this, and it reflects the evidence, but this does not explain why there would be an *increase* in the in-service additions in 2020 for System Renewal work. A reduction in 2020 capital expenditures should not equal an increase in 2020 in-service additions.

Since Hydro One has not provided a narrative to explain any adjustments, except for saying that it has translated the approved capital expenditures into in-service addition reductions, SEC lacks sufficient information to understand what Hydro One has done that would cause the 2020 System Renewal in-service additions to increase. If it is related to the timing of previously forecast 2019 in-service additions, then SEC's comments related to the same issue identified with the other categories of spending applies equally to the System Renewal category.

Capital In-Service Variance Account. Hydro One is requesting the Board modify the terms of the Capital In-Service Variance Account ("CISVA") because of the on-going COVID-19 emergency. Specifically, Hydro One is requesting, presumably due to an expected reduction in completed capital work in 2020 due to the pandemic, that the 2020 and 2021 test years would be calculated together.

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[3] *Ibid.*
[4] DRO, Exhibit 1.2
[5] DRO, p.14, Table 4
[6] DRO, p.18, Table 5

This would mean that if the total 2020 and 2021 approved in-service additions are completed by the end of 2021, whatever year it occurs, there would be no entry into the account.

SEC objects to this modification on two grounds.

First, SEC notes that it is not appropriate to seek what is essentially a motion to review to vary a Board Decision in a draft rate order process. The purpose of the draft rate order process is to implement the Board's Decision into final rates.

Second, if the Board wishes to consider the proposal due to the unique COVID-19 situation, it should be rejected on its merits.

Under Hydro One's proposal, if for example, there is a 10% reduction in in-service additions in 2020, but that work is completed in 2021, Hydro One gets the benefit, and customers pay, as if the work was completed in 2020. This is contrary to the purpose of the account. The CISVA was intended to protect customers, not just from Hydro One undertaking less capital work (in-service additions) than was approved, but also if that work is delayed during the rate period. It should not matter if the variance is due to Hydro One's inability to execute on its plan for more common reasons, or a global pandemic, such as COVID-19. If certain work is not completed in 2020, through the CISVA, customers should not pay as if it had.

The unfairness of the request is magnified considering that the Board has put in place a generic deferral account to capture all of Hydro One's incremental costs and lost revenue caused by COVID-19[7], with the possible recovery of some or all of those amounts.[8] In these circumstances, it would be especially unfair after approving an account to capture increased costs caused by the pandemic, the Board then significantly alters a protection mechanism for customers of the reduced capital work to occur in 2020 also due to the pandemic.

Hydro One's proposal will *over-compensate* the company at the expense of its customers. With that said, if Hydro One's view is that CISVA may *under-compensate* it if it catches up on capital work in later years, then that is not what SEC believes the account was intended to do. Using the above example, if Hydro One completes 10% of 2020 capital work in 2021 (and 100% of its 2021 in-service additions), it should not lose the entire revenue requirement related to that capital work for each of 2020, 2021 and 2022. If it did, then it is correct that it would unfairly be under-compensated. What would be fair in that scenario is that the CISVA account would record, a) the 2020 revenue requirement related that 10% difference in in-service additions and, b) in 2021, the revenue requirement difference of that 10% capital in-service for the full year versus being added during the year. Hydro One should be able to catch up on work that is delayed, but it should not be able to be compensated as if it had completed the work on time.

Regulatory Taxes. SEC has reviewed the new calculations of regulatory taxes, and the increase in revenue requirement that Hydro One says results from those calculations, both in some detail, but we have been unable to confirm that those calculations are accurate or reasonable.

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[7] OEB Letter Re: Accounting Order for the Establishment of Deferral Accounts to Record Impacts Arising from the COVID-19 Emergency for Ontario Power Generation Inc. and Electricity Transmitters, dated April 29, 2020
[8] OEB Letter, Re: Consultation on the Deferral Account – Impacts Arising from the COVID-19 Emergency (EB-2013-0133), dated May 14, 2020

With respect to the tax shield associated with capital assets, it is true that in the first one or two years an asset is in-service, its net impact on revenue requirement may be reduced, because the tax shield (tax savings from CCA) exceeds the cost of capital plus depreciation for those new assets. This differs from one asset class to another, and it is exacerbated by the recent Accelerated CCA provisions added to the *Income Tax Act.*

The Board has been provided with no information on how the allocation of the capital spending reductions to asset classes affects this tax shield. Depending on the asset class, some assets produce more tax shield than others, because the difference in deduction rate between depreciation and CCA is higher. Further, since only part of the reduction in capital expenditures is reflected in reduced in-service additions ($100M less than the capital expenditures), the reduced capital expenditures do not reduce ROE and therefore, taxable income and regulatory taxes to the same extent.

SEC is also unable to recreate the $56.4M of CCA lost due to the Decision, as set out in Exhibit 1.5. Particularly problematic is the $42.1M of reduced CCA in 2021, for which we have found no explanation, and seems to be anomalous. While we looked closely at Exhibit 1.5.2, it does not show the impacts of the Decision on the line items, and we do not appear to have a comparable table immediately before the Decision to which we can compare each line. If Exhibit 1.5.2 followed the pattern of other Exhibits and showed pre-Decision, the impact of Decision, and DRO figures in each case, it would be possible to see how the calculation is being done. As it is, the Board is being shown the result and not the calculation of the delta.

With respect to OPEBs, from a tax point of view, the tax should be the same whether OPEBs are treated as operating costs or capital expenditures. However, from a regulatory point of view, shifting OPEBs to operating costs increases revenue requirement, but the tax liability remains the same. This means that from a regulatory point of view there is a tax shield lost. To put it in concrete terms, on Exhibit 1.5.1, any amounts in lines 14 or 15 that are no longer capitalized do not affect the regulatory net income (they do not reduce the utility's margin; they simply increase rates dollar for dollar), but they are no longer available on lines 14 or 15, and so they increase taxable income and therefore regulatory tax payable.

SEC has attempted to reconcile the OPEBs changes in Table 6 of the DRO with the adjustments to the tax shield, but we have been unable to do so. Exhibit 1.5.1, like Exhibit 1.5.2, does not show the impacts of the Decision in the line items.

Finally, Exhibit 1.5 has a line "Other Timing Differences" which shows increases in taxable income of $29.5M, $30.2M, and $31.0M in each of 2020, 2021, and 2022. SEC could not find a calculation of those figures and cannot recreate them from baseline information. Those three figures represent about two-thirds of the $43M increase in regulatory income taxes claimed, and thus two-thirds of the $58.5M increase in rates because of tax calculations. Some portion of that is likely OPEBs, but certainly not all of it.

SEC requests Hydro One addresses these deficiencies in its reply submissions and provide the necessary support for its calculations.

Transmission Scorecard. Hydro One has implemented the Board's Decision on the Transmission Scorecard by providing the details about the newly renamed Transmission Capital Accomplishment

Index (“TCAI”).[9] SEC notes that as TCAI involves a calculation that includes a comparison of planned and replaced units and their budgets to actual units replaced, it is important for the baseline planned units and budgets to be provided upfront. Considering the planned budgets and units in the application are likely to be different because of the reductions ordered by the Decision, Hydro One should be required to file the revised planned units and budgets for each program that the actual accomplishments will be compared against.

Rate Implementation Option. Hydro One has proposed several implementation rate options. SEC’s member schools are not transmission-connected customers, and so will not see the change in UTRs on their bills until January 1, 2021, when distributors RTSR’s are adjusted. Because of that, we cannot comment on the appropriateness of any proposal to implement the UTRs as of January 1, 2021, instead of July 1, 2021 (‘Decision’ and Alternative 1). Between Alternatives 2 and 3, SEC prefers Alternative 3, as we agree with Hydro One that it would be better to spread the 2020 foregone revenue over the two remaining years of the rate plan instead of over one year, especially with other potential rate increases that may occur on a customer’s electricity bill in 2021 due to COVID-19.[10] Regardless of which option is chosen, the Board should not allow Hydro One to accrue additional interest on the balance as of July 1, 2021, which is when rates could be implemented.

Yours very truly,
Shepherd Rubenstein P.C.

Mark Rubenstein

cc: Wayne McNally, SEC (by email)
Applicant and intervenors (by email)

[9] DRO, p.32-34
[10] For example, the Government of Ontario has announced that they will begin recovering the deferred Global Adjustment amounts over 1-year beginning in January 2021.