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File 92867

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VIA RESS FILING and EMAIL: registrar@oeb.ca

Christine E. Long,
Registrar
Ontario Energy Board
2300 Yonge Street
27th Floor
P.O. Box 2319
Toronto, ON M4P 1E4

Dear Ms. Long,

Re: Hydro One Networks Inc. - Transmission Revenue Requirement and Distribution Revenue Requirement and Tax Issue – Future Tax Savings (EB-2020-0194)

Attached please find the Submissions of the Power Workers' Union in connection with the above-noted proceedings. An electronic copy has been filed through the Board's RESS filing system.

Yours very truly,
PALIARE ROLAND ROSENBERG ROTHSTEIN LLP

Richard P. Stephenson
RPS:pb

Attach.

Doc 3651575 v1

EB-2020-0194

Hydro One Networks Inc. Transmission Revenue Requirement and Distribution Revenue Requirement and Tax Issue – Future Tax Savings

Submission of the Power Workers' Union (PWU)

Introduction

On October 28, 2015, Hydro One exited the PILS Regime when the Province ceased to own 90% of its ownership interest in the company.

On May 31, 2016, Hydro One applied for approval of the 2017 and 2018 rates revenue requirements for its transmission business (EB-2016-0160) (Original Application). The applied-for amounts included the recovery of forecast income taxes calculated on a basis consistent with the provincial payment in lieu of taxes regime (PILS Regime), which was the tax scheme in place when Hydro One was owned outright by the Province of Ontario. Hydro One correctly understood that payment of the PILS Departure Tax was a consequence of the Province's decision to sell a portion of its ownership interests and not a cost related to the provision of rate regulated services. As a result, Hydro One did not seek to recover the PILS Departure Tax from ratepayers in its Original Application and, in turn, Hydro One did not propose to provide any allocation of the Future Tax Savings that would arise from the transaction to ratepayers in the Original Application.

On September 28, 2017 (revised October 11 and November 1, 2017), the Board issued the Original Decision, in which it determined that a portion of Future Tax Savings should be allocated to ratepayers. The effect of the Original Decision was to reduce the amount of income tax Hydro One was permitted to recover in its transmission revenue requirement (and consequently its rates) for the period January 1, 2017 to December 31, 2018. That impact was extended and carried forward in the Board's rate determinations for both Hydro One transmission and distribution for each rate period since that time.

On July 16, 2020, the Divisional Court of Ontario overturned the Board's Original Decision and instructed that no portion of the Future Tax Savings should be allocated to ratepayers and that no part of the benefit of the Future Tax Savings is allocable to ratepayers and should instead be paid to the shareholders in its entirety. The Board did not appeal that decision.

On October 2, 2020, the OEB issued Notice and Procedural Order No. 1 (PO#1) in the current proceeding to implement the Decision of the Court. The PO#1 also directed

Hydro One to file evidence on matters related to implementing the Court's decision and Hydro One did so subsequently.

The consequence of the Board's errors in the Original Decision was that Hydro One was wrongly deprived of incremental revenues in respect of both of its transmission and distribution businesses for the period since January 1, 2017. The issue in this proceeding is to seek to properly compensate Hydro One from the losses it incurred as a result of the Board's error.

The following is PWU's submission on selected sections of Hydro One's evidence, organized in accordance with the applicable sections used by Hydro One in its application evidence.

3.1 Calculation of Misallocated Tax Savings Amounts

The PWU submits that Hydro One has complied with the requirements of PO#1 by filing misallocated tax savings amounts divided between its transmission and distribution businesses for each of the relevant rate orders since January 1, 2017 as follows:

Table 1: Misallocated Tax Savings Amounts Deducted from Regulatory Income Tax[1]

Year	Transmission	Proceeding	Distribution	Proceeding
2017	$31.2M[4]	EB-2016-0160	-[5]	N/A
2018	$35.1M[6]	EB-2016-0160	19.3M[7]	EB-2017-0049
2019	$35.4M[8]	EB-2018-0130	26.3M[9]	EB-2017-0049
2020	$32.8M[10]	EB-2019-0082	24.2M[11]	EB-2017-0049
2021	$30.5M[12]	EB-2019-0082	22.5M[13]	EB-2017-0049
Total for 2017-2021	**$165.0M**		**$92.4M**[14]	

3.1.1 Recovery of Carrying Costs During the Appeal Period

Given that a period of four years elapsed between the effective date of the Original Decision and the conclusion of the ensuing appeal process, there is no question that Hydro One should be compensated for the lost time value of money that resulted from the Board's erroneous Decision. To that end, Hydro One considered three carrying cost rates, viz., the OEB Prescribed Rates (Quarterly rate), the Weighted Average

[1] Exhibit A, Tab 1, Schedule 1, Page 7 of 20

Cost of Debt (WACD), and Weighted Average Cost of Capital (WACC).[2] The carrying costs, by year up to 2021 under each of the potential rates, are presented as follows:

Table 3: Carrying Costs[3]

($M)	2017	2018	2019	2020	2021[18]	TOTAL
OEB Prescribed Rates						
Transmission	0.2	0.9	1.9	1.6	0.9	**5.4[19]**
Distribution	0.0	0.2	0.7	0.7	0.5	**2.1**
Weighted Average Cost of Debt (WACD)						
Transmission	0.7	2.2	3.8	5.1	6.5	**18.3**
Distribution	0.0	0.4	1.4	2.5	3.5	**7.8**
Weighted Average Cost of Capital (WACC)						
Transmission	0.9	2.7	4.7	6.3	8.0	**22.5[20]**
Distribution	0.0	0.5	1.8	3.2	4.5	**10.0**

Hydro One ruled out the use of OEB prescribed rates of interest since they are applied in normal course utility operations involving the deferral account variances and construction work in progress matters whereas the matter at hand involves the payment of monies made under errors of law and impacted by lengthy appeal periods.[4]

Hydro One submitted that, in the present circumstances, its weighted average cost of debt (WACD) is the appropriate rate used to calculate all carrying costs because, as a result of the Original Decision, Hydro One incurred a higher level of debt than it otherwise would have. Hydro One adds that the WACD is the most appropriate carrying charge because the Misallocated Tax Savings Amounts were funds otherwise expected to be received by Hydro One in its normal operations. The cost to finance this shortfall would reasonably attract Hydro One's WACD given that it was over a [four] year period.[5] The PWU notes that the shortfall happened over a period of 5 years and not 4 years. Applying the Hydro One proposed OEB approved WACD would result in a carrying cost of $26.1M, making the total amount of misallocated tax savings to be recovered $283.5M.

Hydro One's evidence does not discuss the reasons why Hydro One ruled out the third carrying cost rate it considered: the Weighted Average Cost of Capital (WACC). Hydro One, however, makes a reference to two decisions by the Alberta Utilities Commission: One in which the Commission applied the Bank of Canada rate plus 150

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[2] Ibid. Page 8 of 20
[3] Ibid.
[4] Ibid. Page 9
[5] Ibid. Page 10

basis points, and another in which the Commission applied the WACC. With respect to the latter, Hydro One stated:

> **That said, Hydro One observes that in circumstances where the issue of carrying costs associated with the refund of imprudently incurred costs to customers is in issue, the Alberta Utilities Commission has approved the use of the utility's weighted average cost of capital in calculating carrying costs included in the overall amount returned to ratepayers. The Commission's designated interest rate used for the purpose of calculating deferral account variances was not selected given the different and unique circumstances associated with a customer refund resulting from costs that were determined to be imprudently incurred as compared to normal course variance account operations.[6]**

The PWU notes that Board staff, in their submission, disagreed with Hydro One's proposed use of approved WACD. OEB staff submitted that the prescribed CWIP rate, or alternatively, the BoC + 150 bp rate, would be the appropriate carrying charge rate.[7] Board staff argues that unlike the WACD, which is based on a long-term rate, a mid-term rate [such as the prescribed CWIP] would be appropriate and correspond to the five-year appeal period (2017-2021).[8] Moreover, Board staff submits that the carrying charge rate applicable to this case should reflect the time value of money corresponding to the period in which Hydro One did not have the funds relating to the Future Tax Savings; "in other words, this can be viewed as Hydro One lending funds to ratepayers for a five-year period, from 2017 to 2021 (recovery of Future Tax Savings is proposed to commence in 2021)."[9]

It is not clear to the PWU how the period in which Hydro One did not have the funds relating to the Future Tax Savings is reduced only to the 5-year appeal period (2017-2021). It is true, the appeal period is 5-years long. However, Hydro One is not proposing to recover the full amount of the Misallocated Tax Savings in 2021. Rather, it proposes to do so over the whole of the 2021-2027 period. Board staff supports this proposal. As a consequence, the period in which Hydro One would not have the funds relating to the Future Tax Savings is not five years – it is the entire period of time until the recovery process is complete (i.e., until 2027).

Board staff appears to treat the 2017-2021 appeal period separately from the 2021-2027 recovery period so as to make the duration of the under-recovery look short enough to justify the CWIP approach. In reality, and, if the Board accepts the proposed recovery time, it would have taken 11 years for Hydro One to recover the Misallocated Tax savings.

[6] Ibid. Page 9
[7] Board staff submission, Page 9
[8] Ibid. Page 10
[9] Ibid. Page 9

Similarly, Board staff's characterization that the situation can be viewed as Hydro One "lending funds" to ratepayers for a five-year period, from 2017 to 2021, is not reasonable because the Board's decision was not to defer recovery for 5 years, it was rather that Hydro One would never recover the tax savings from ratepayers. Normally, that would effect a different type of decision by Hydro One - to arrange financing, consistent with the Misallocated Tax savings, which could not be arranged through a 5-year loan at the CWIP rate. Hydro One would need to acquire the financing in the amount of the Misallocated Tax Savings to make the company whole.

More fundamentally, it is the PWU's submission that the characterization of the circumstances as Hydro One "lending funds" to ratepayers is inaccurate. The fact of the matter is that the Board's Original Decision unlawfully allocated tax savings to ratepayers. The Divisional Court remedied the wrong and determined that no part of the Future Tax Savings is allocable to ratepayers and should instead be paid to the shareholders in its entirety because the amounts do not pertain to the provision of rate regulated service and thus fall outside of the calculation of rates. It was Hydro One's shareholders who were wrongly deprived by the Board's erroneous decision. The object of the current process should be to make the injured party "whole" for the losses it incurred. Viewed through this lens, the focus should not be on Hydro One's actual or imputed debt rates, but rather on Hydro One's return on equity. The effect of the Board's erroneous decision (as Board Staff notes) was not to increase the borrowing that Hydro One had to undertake to finance its operations, but rather to improperly reduce its shareholder's return.

In the PWU's submission, the appropriate carrying charge rate should have been the Board-approved return on equity, which would have resulted in higher rates and hence higher recovery amounts. Any other measure fails to make the injured party "whole".

The PWU is mindful that the loss here was caused by the Board, not the ratepayers,[10] and it will be ratepayers who will be making up this loss. As a consequence, it may be appropriate for Board to consider an approach which does not visit the full costs of making Hydro One whole on ratepayers. In view of the true measure of its losses, Hydro One's proposal to use the WACD is fair and balanced and therefore, should be approved.

3.1.2 Carrying Costs Incurred During the Recovery Period

For the same reasons discussed under 3.1.1 above, the PWU supports Hydro One's proposal to use the WACD for carrying charge rate. The PWU also supports Hydro One's proposal to establish two accounts to accomplish the recovery.

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[10] Although ratepayer groups did advocate and defend the Board's erroneous approach.

3.1.4 Options for Recovering Misallocated Tax Savings Amounts

Hydro One has proposed three options for recovering misallocated tax savings:

Option 1 – Recovery over 2021 and 2022

Option 2 – Recovery from 2021 to 2024

Option 3 – Recovery from 2021 to 2027 (Hydro One recommended option)

The PWU supports the Hydro One-recommended Option 3, which would see the amounts to be recovered from customers over a seven-year period, because it balances the Divisional Court's decision that Hydro One's shareholders must be kept whole with the objective that rate impacts on customers are reasonably mitigated.

All of which is respectfully submitted.