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Feb. 26, 2021

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

Dear Ms. Long,

RE: EB-2020-0194 - London Property Management Association Submissions for Hydro One Networks Inc. – 2017-2022 Transmission Revenue Requirement and Charge Determinants and 2018-2022 Distribution Revenue Requirement and Rates, Remittal of Future Tax Savings Issue

1. INTRODUCTION

The following are the comments of the London Property Management Association ("LPMA") related to the remittal of future tax savings related to Hydro One Networks Inc. ("HONI") 2017-2022 transmission revenue requirement charge determinants and the 2018-2022 distribution revenue requirement and rates.

A decision of the Divisional Court of Ontario ("Divisional Court") dated July 16, 2020 overturned the Ontario Energy Board's ("OEB" or "Board") EB-2016-0160 Decision and Order that concluded that a portion of the future tax savings resulting from the Government of Ontario's decision to sell a portion of its ownership interest in Hydro One Limited by way of an Initial Public Offering on October 28, 2015 and subsequent sale of shares should be applied to reduce HONI's transmission revenue requirement for 2017 and 2018.

This reduction in HONI's transmission revenue requirement was incorporated into 2019 through 2022 subsequent OEB decisions (EB-2018-0130 for 2019 and EB-2019-0082 for 2020 through 2022). It was also incorporated into HONI's distribution revenue requirement for 2018 through 2022 in the EB-2017-0049 proceeding.

The Divisional Court found that no portion of the future tax savings should have been allocated to ratepayers when the evidence was clear that HONI paid all of its costs under the stand-alone utility principle and that no part of the benefit of the future tax savings was allocable to ratepayers and should be paid to the shareholders in its entirety.

The OEB initiated the current proceeding on October 2, 2020 when it issued a Notice and Procedural Order No. 1 stating that this proceeding was being established to implement the direction of the Provincial Court that all of the future tax savings should be allocated to Hydro One's shareholders.

2. THE ISSUES TO BE DETERMINED

a) Calculation of Misallocated Tax Savings 2017 – 2021

LPMA submits that HONI has provided the misallocated tax savings for the period 2017 through 2021 for both the transmissions and distribution business in Table 1 of Exhibit A, Tab, Schedule 1. Further, LPMA accepts the approach used by HONI to calculate these misallocated tax savings and the resulting figures shown in Table 1.

b) Carrying Costs

LPMA submits that the Board should not include any carrying costs associated with the recovery of the misallocated tax savings. There are several reasons for this submission.

First, LPMA submits that it is not appropriate for customers to pay carrying costs on the repayment of an amount that was no fault of their own.

In the RP-2002-0147/EB-2004-0004 application by Natural Resource Gas Limited ("NRG"), the OEB dealt with a similar issue. NRG had identified that the Purchased Gas Commodity Variance Account ("PGCVA") did not fully account for the difference between actual gas costs and the gas costs reflected in rates. The PGCVA mechanism was deficient and resulted in NRG collecting less from customers than it should have.

In the RP-2002-0147/EB-2004-0004 Decision and Order dated April 19, 2004 the Board stated that *"…while we accept that the NRG's customers have underpaid by $531,794 and the 2003 PGCVA balances have not been finalized by the Board, we find that NRG's error has resulted in a substantial and avoidable accumulation of potential customers' charges,* ***through no fault of the customers****"* and went on to state that *"****We must therefore look for a balance.****"* (pages 5-6) (emphasis added)

At page 6 of the decision, the Board allowed NRG to recover the prudently incurred unrecorded gas costs of $531,704 and went on to state that *"It is also our view that **customers should not be burdened by any interest charges** that would not have accrued had the customers been presented with the appropriate timely billing."* (emphasis added)

In summary, the Board determined that customers should not be burdened by any interest charges on the amounts to be paid to the utility as the result of its error.

While not exactly comparable to the situation in the current proceeding, LPMA submits that customers should not be burdened by any interest charges on the amounts to be paid to the utility as a result of the Board's error.

In the response to Exhibit I, Tab 1, Schedule 2, part (d), HONI states that:

> *"The injured parties are Hydro One's shareholders; parties who are not directly involved in the rate setting process. During the Recovery Period, Hydro One shareholders would continue to suffer the effects of the time value of money in the same manner as they had sustained when the misallocations occurred. The longer the recovery period, the greater the potential exists for Hydro One and its shareholders to receive less than the amount they would have received had the Original Decision correctly determined the matter in accordance with the Divisional Court's reasoning."*

While LPMA has some sympathy for the shareholders, it should be noted that the customers are also parties who are not directly involved in the rate setting process and they should not be penalized with additional carrying costs for the Board's error when in a similar instance, the Board determined that the customers of NRG were not to be burdened with additional carrying costs for the utility error. In both instances, the customers are innocent bystanders and regardless of who made the error, should not be expected to pay for it.

LPMA also notes that in the response noted above, HONI correctly indicates that the longer the recovery period, the greater the potential exists for HONI and its shareholders to receive less than the amount they were entitled to in the absence of the Board error. LPMA provides submissions later on with regard to the recovery period, and essentially submits that shorter recovery periods reduce the costs to customers through significant reductions in carrying costs. LPMA also notes that the shorter the recovery period, the better off will be the shareholders, creating a win-win situation.

Second, as indicated in the response to Exhibit I, Tab 2, Schedule 1, the Divisional Court did not make any determination on compensation/payment to HONI related to carrying costs. HONI agreed that the Divisional Court found that matters concerning the implementation of its decision included only the calculations and method of recovering of the Misallocated Tax Savings were remitted to the OEB.

Third, HONI has not provided any evidence that it incurred incremental debt to finance the misallocated tax savings. LPMA agrees with the Staff submission (dated February 22, 2021 at page 9 that:

> *Hydro One stated that, as a result of the Original Decision, it has incurred a higher level of debt than it otherwise would have incurred. Hydro One further stated that the approved WACD is appropriate because the amount of Future Tax Savings were funds it otherwise expected to be received in normal operations and the cost to finance this shortfall would attract Hydro One's WACD, given that it was over a four-year period.22,23 OEB staff disagrees with this characterization. In the Original Decision (and associated subsequent decisions), the reduction of revenue requirement for the Future Tax Savings did not impact the OEB's decision on Hydro One's capital program and projects, or the financing of these projects and the refinancing of existing assets. As a result, approved Uniform Transmission Rates (UTRs) and distribution rates reflected the appropriate level of debt financing/refinancing costs for Hydro One and were compensatory to allow Hydro One to recover its cost of capital, including any additional debt incurred as a result of the Future Tax Savings allocation.*

Fourth, HONI did not have any deferral or variance account associated with the misallocated tax savings. If such an account had been in place, then interest at the prescribed interest rate, or some other Board approved rate, could have been included as part of the accounting order. However, no such account was approved by the Board.

Fifth, there is a great deal of intergenerational inequity associated with the recovery of carrying costs. Customers that benefited through lower rates in 2017 through 2021 will not be the same customers that would pay the carrying costs, especially if the Board were to approve a long recovery period. Not only will some customers in the 2017 through 2021 period no longer be customers in all or any of the recovery period, there will also be a significant number of customers in the recovery period that were not customers in the 2017 through 2021 period. In other words, for a significant number of customers, the costs will not align with the benefits. While this is unavoidable with respect the amount of the misallocated tax savings to be recovered, the Board can reduce the intergenerational inequity by eliminating the incremental carrying costs.

Finally, HONI states (Exhibit I, Tab 1, Schedule 2, page 4) that because the misallocated tax savings amounts do not pertain to the provision of rate regulated services and do fall outside of the calculation of rates, then the misallocated tax savings cannot be characterized as a "regulatory" asset and subject to deferral and variance account treatment. If this is the case, then LPMA submits that the Board is under no obligation to approve any carrying costs that fall outside of the calculation of rates.

If the Board were to determine that carrying costs should be recovered from customers, even though those customers were not at fault for the Board error, then LPMA submits that the Board should direct HONI to calculate the carrying costs based on the Board's prescribed interest rate.

LPMA believes that the amounts to be recovered should be treated in the same manner as amounts in the new sub-account under Account 1592 which HONI was directed to establish. This new sub-account records the revenue requirement impact of changes in capital cost allowance rules. Carrying charges on this account are at the prescribed interest rate.

Most importantly, LPMA submits that the Board should do everything in its power to mitigate the costs to customers associated with the Board error. As the following table shows, there is a significant difference on the costs to customers of using different interest rates (and different recovery periods). For example, under Option 3 of a 2021 through 2027 recovery period, the carrying cost ranges from $5.3 million using the OEB prescribed rate to $49.9 million using the weighted average cost of capital. Using the weighted average cost of debt, as proposed by HONI, results in additional costs to customers of $40.3 million.

Much of this increased cost will be borne by customers throughout 2022 through 2027 that did not receive any benefit of lower rates in 2017 through 2021. The Board can minimize this intergenerational inequity by doing two things: shortening the recovery period and using the OEB prescribed interest rate. As shown in Table 1, the total cost under Option 1 of a 2021 through 2022 recovery period and using the OEB prescribed interest rate, the carrying cost is $1.6 million. The difference between this figure and the $40.3 million figure noted above is substantial.

Table 1 - Carrying Costs

Interest Rate		Option 1 2021-2022 Recovery	Option 2 2021-2024 Recovery	Option 3 2021-2027 Recovery
OEB Prescribed Rate	Transmission	1.1	2.0	3.4
	Distribution	0.5	1.2	1.9
	Total	1.6	3.2	5.3
Weighted Average Cost of Debt	Transmission	8.0	15.0	25.7
	Distribution	4.5	8.5	14.6
	Total	12.5	23.5	40.3
Weighted Average Cost of Capital	Transmission	9.8	18.6	31.5
	Distribution	5.7	10.8	18.4
	Total	15.5	29.4	49.9
Bank of Canada plus 150 Basis Points	Transmission	3.9	7.4	12.6
	Distribution	2.2	4.2	7.0
	Total	6.1	11.6	19.6
Board Approved Short Term Debt Rate	Transmission	5.1	9.6	16.4
	Distribution	2.4	4.5	7.7
	Total	7.5	14.1	24.1

Source: Exhibit I, Tab 2, Schedule 3, pages 3 - 5

c) Recovery Period for 2017-2021 Misallocated Tax Savings

LPMA supports a start date for the recovery period that is as soon as possible, in order to minimize carrying costs for customers. Beginning the recovery as soon as possible will also help with rate mitigation.

LPMA notes that there is no reason for the recovery periods to be the same for the transmission and distribution components of the misallocated tax savings. HONI confirmed this in the response at Exhibit I, Tab 2, Schedule 5. LPMA submits that the Board should consider different recovery periods for each of the transmission and distribution portions of the misallocated tax savings.

i) Transmission Recovery Period

LPMA supports the recovery of the transmission amounts effective July 1, 2021, assuming the Board can reset the revenue requirement UTR pools and allocation factors in time to do this. LPMA does not believe that there should be any impediment to this timing.

LPMA supports a short recovery period for the transmission portion of the misallocated tax savings. Specifically, LPMA supports recovery of these amounts over a two-year period. If the transmission rates are changed effective July 1, 2021, this would result in recovery of the transmission related misallocated tax savings being split over 3 rate years, with 25% recovered in 2021, 50% in 2022 and 25% in 2023.

As shown in Table 5 in Exhibit A, Tab 1, Schedule 1, the bill impact on a distribution residential customer of recovering the transmission portion of the misallocated tax savings is less than 1% in the first year and only 0.3% in the second year and would be felt by the customers with a one-year lag, given the timing of implementing changes to transmission rates in the setting of distribution retail transmission charges. With the recovery split over three rate years rather than two, it is expected that these figures would be lower on a yearly basis.

LPMA notes that the bill impact is lower the longer the recovery period is. However, the longer the recovery period is, the higher is the total cost to the customers through the addition of extra carrying costs. Clearly there is a trade off between the rate/bill impact and the cost impact. LPMA submits that a two-year recovery period for the transmission portion of the misallocated tax savings provides a minimal rate/bill impact along with cost minimization.

As shown above in Table 1 above, there is a significant additional cost to customers of extending the recovery period from 2 years to 4 years or to 7 years. Under HONI's proposal to use the weighted average cost of debt, the transmission related carrying cost nearly doubles from $8.0 million in the two-year option to $15.0 million in the four-year option. Extending the recovery over seven years more than triples the cost to $25.7 million. Regardless of the interest rate used to calculate the carrying charge LPMA submits that the Board should minimize the cost to customers and recover the transmission portion of the misallocated tax savings over a two-year period.

Similarly, and again to minimize the cost to customers, LPMA does not support waiting until January 1, 2022 to start recovery of the misallocated tax savings in the event that the

OEB approves some level of carrying costs. Deferring the start of the recovery period would only result in higher costs to be borne by customers as a result of the Board error.

ii) Distribution Recovery Period

LPMA is not making any specific submissions with respect to the recovery period associated with the distribution portion of the misallocated tax savings as there are few, if any, LPMA members served by HONI distribution. However, LPMA again notes the trade off between costs and bill/rate impacts. Given that the costs are a direct result of a Board error, LPMA submits that the OEB should minimize the costs to customers while ensuring that the rate/bill impacts are reasonable. Table 1 above also highlights the impact of the carrying costs on distribution customers associated with the three recovery periods.

With respect to the distribution amounts, LPMA submits that an appropriate time to begin recovery these amounts should be no later than November 1, 2021, when the time-of-use rates are adjusted. Again, the sooner the amounts begin to be recovered, the less the total cost will be to customers.

LPMA also notes that the Board could direct HONI to have different recovery periods for different distribution rate classes, depending on the rate/bill impacts. This would allow for cost minimization associated with carrying costs for all rate classes where the rate/bill impacts of a shorter recovery period result in acceptable rate/bill impacts.

e) Calculation of Misallocated Tax Savings 2022

HONI proposes to amend its method of calculating regulatory income taxes included in the base revenue requirement by removing line-item deductions attributable to the future tax savings amounts of $28.4 million for transmission and $21.0 million for distribution. These values, along with their sources are shown in Table 8 of Exhibit A, Tab 1, Schedule 1.

LPMA supports they HONI proposal and the amounts shown. This approach would stop the misallocation of tax savings flowing to customers effective for 2022 and would eliminate the need for ratepayers to repay HONI at a later date, potentially with added interest costs.

f) Summary of Recommendations

LPMA recommends that the Board disallow carrying costs on the misallocated tax savings, or failing that, using the OEB's prescribed interest rate, and direct HONI to recover the amounts over the shortest time period that does not result in significant rate increases in any year. This may result in different recovery periods for the transmission and distribution ports of the misallocated tax savings and different recovery periods by rate class. This is a win-win situation that would minimize the costs for customers while providing the funds to the company and its shareholders in a short period.

3. COSTS

LPMA requests that it be awarded 100% of its reasonably incurred costs. LPMA submits that it has acted responsibly and efficiently in all aspects of the process.

Yours very truly,

Randy Aiken Digitally signed by Randy Aiken
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c.c. Hydro One Regulatory (e-mail only)