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August 31, 2021
Our File: EB20210169

Attn: Christine Long, Registrar

Dear Ms. Long:

Re: EB-2021-0169 – Hydro One ATP Account – SEC Submissions

We are counsel to the School Energy Coalition ("SEC"). Pursuant to Procedural Order No.1, these are SEC's submissions on the application by Hydro One Networks Inc. ("Hydro One") for approval to establish the proposed Affiliate Transmission Projects Account ("ATP Account").

As discussed in these submissions, SEC submits the Board should deny approval of the proposed ATP Account. Hydro One's proposal is inconsistent with the existing approved transmission rate framework that is in place until the end of 2022. Furthermore, it is neither needed nor appropriate.

Background

Hydro One has proposed the establishment of the ATP Account, which is to record, in two separate sub-accounts, certain costs related to transmission projects that a) Hydro One will develop and/or construct as a result of a letter from the Independent Electricity System Operator ("IESO") identifying a transmission need, and/or an Order-in-Council directing the OEB to amend its license requiring it to do so, and b) it expects it will, in whole or in part, be owned by and included in the rate base of a new partnership who will be a separately licensed transmitter.[1]

The latter requirement is part of Hydro One's laudable corporate strategy of entering into equity partnerships with Indigenous communities for new large-scale transmission developments. SEC strongly supports that strategy, and nothing in these submissions should be interpreted as suggesting that it be weakened or reduced. SEC's submissions are about the appropriate regulatory treatment of certain costs within Hydro One's currently approved regulatory framework, not the social and economic policy goals advanced by these arrangements.

The proposed ATP Account would have two separate sub-accounts that will be treated differently. The first sub-account (ATP-Project Development Engineering and Planning Work deferral account) would be a deferral account and would capture development costs incurred prior to the point where

[1] Application, p.1

capitalization is appropriate.[2] When a project does reach the point where capitalization is appropriate, the costs would be transferred to the project's CWIP Account. If the recorded costs are not ultimately capitalized because the transmission project does not go forward, regardless of whether a new partnership was ultimately created, Hydro One would be eligible to seek recovery of the related balance.[3]

The second sub-account (ATP - Project Construction Costs tracking account) is to track all construction costs related to the eligible projects. This includes development, engineering, and planning costs that may have previously been included in the first sub-account, but now are eligible to be capitalized.[4]

SEC understands the proposal to be that this proposed sub-account is neither a deferral nor a variance account, but a 'tracking' account". The distinction is that the balance in this sub-account is not eligible to be recovered from ratepayers, and is recorded for the purpose of greater transparency.[5] The balance in this 'tracking' sub-account related to an eligible project will be the same as the project's CWIP account.[6]

Adding confusion, while Hydro One uses the term tracking account, the Draft Accounting Order's specific wording appears to indicate that the sub-account *may* turn into a deferral account, if the project does not go into service. At that point, the "sub-account no longer functions as a 'tracking' account" and "[t]he balance would be held in this account until Hydro One can apply to the Board for disposition in a future rate rebasing application."[7]

The expectation is that, if the assets are constructed, the costs will be recovered in the initial rate application of the new partnership. Hydro One does not plan to include any completed projects eligible for the proposed account in future transmission rate applications.

This application is brought in the middle of Hydro One's approved multi-year regulatory framework for the recovery of costs of its transmission business. In EB-2019-0082, the Board approved a Custom IR rate framework that will govern Hydro One from 2020 through to the end of 2022.[8] The framework includes a number of components, such as an annual revenue requirement adjustment, and various available mechanisms, if Hydro One believes it requires additional funding. This includes access to a Z-Factor, with a specific event-related materiality threshold, and access to a regulatory off-ramp that the OEB may initiate if its ROE is +/-300 basis points from the approved level.[9] In addition, the OEB approved both continuation and the establishment of a lengthy list of deferral and variance accounts.[10]

Hydro One has not identified any provision of its approved rate framework which allows for the approvals sought in this application.[11]

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[2] Application, p.4
[3] Application, p.5
[4] Application, p.17
[5] Interrogatory Response OEB Staff#2(a)
[6] Interrogatory Response EP #4(b)
[7] Application, p.18
[8] *Decision and Order* (EB-2019-0082), April 23, 2020
[9] *Decision and Order* (EB-2019-0082), April 23, 2020, p.42
[10] *Decision and Order* (EB-2019-0082), April 23, 2020, p.158-173
[11] Interrogatory Response SEC#1

Approved 2020-2022 Rate Framework Governs Any Application

Hydro One has an approved rate framework for its transmission business, in place until the end of 2022. This application is inconsistent with those approvals, and so should be denied.

SEC's Interrogatory #1 asked directly "[u]nder what aspect of that approved rate framework is Hydro One's basis for the proposed account (e.g., Z-Factor, etc.)?" Hydro One responded by pointing to Chapter 2 of the OEB's Filing Requirements for Electricity Transmission Applications, which sets out the criteria for which an applicant can propose a new deferral and variance account, if specific requirements are met (i.e., materiality, causation and prudence).

SEC submits Chapter 2 is not a valid basis for approval of the ATP Account. The Chapter 2 Filing Requirements are for "Revenue Requirement Applications" (i.e., its Custom IR application in EB-2019-0082), and are not meant for mid-framework applications.[12] If a utility was able to apply for a deferral and variance account at any time, that would entirely undermine the approved multi-year rate framework, which involves a balancing of various components and risks between the utility and its customers, including unforeseen costs.

The appropriate time for Hydro One to apply for the ATP Account is when it seeks approval of its next rate framework. In fact, that is what Hydro One is already proposing.

In its recently filed Joint Rate Application for 2023 to 2027 (EB-2021-0110), Hydro One is seeking approval of what it has called an Externally Driven Transmission Projects Variance Account.[13] The proposed account would capture, among other things, the same types of costs that the ATP Account would capture, but beginning in 2023.[14] In recognition of the current application, Hydro One has proposed a carve-out of the proposed Externally Driven Transmission Projects Variance Account for projects that would be recorded in the ATP Account.[15]

The fact that these projects are planned to be transferred after or near their in-service date to a new partnership, and will not be added to Hydro One's transmission rate base, is of limited relevance. While that may be Hydro One's intention, if the projects are not put in-service the ATP Account balances will be recovered in Hydro One's transmission rates, as there will be no new partnership. Those rates are governed until the end of 2022 by the existing rate framework.

There is irony in Hydro One's approach. In Hydro One's 2020 distribution rate adjustment application (EB-2020-0030), Hydro One forcefully argued that a request from SEC and other parties to make certain corrective adjustments to the approved rate framework formula was out of scope and that the OEB could not consider the issue until the company's next rebasing application.[16] The OEB agreed with Hydro One. The same logic applies here with even more force, since the changes proposed by Hydro One are not even intended to be corrective in nature.

SEC submits the appropriate time to consider establishing the ATP Account is in the context of Hydro One's 2023-2027 Joint Rate Application, where the OEB will consider the appropriate rate framework for the company. That includes any deferral and variance accounts that should be established.

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[12] Filing Requirements For Electricity Transmission Applications, Chapter 2, Revenue Requirement Applications

[13] See EB-2021-0110, Exhibit G-1-2, p.16

[14] *Ibid*

[15] EB-2021-0110, Exhibit G-1-2, p.19

[16] *Decision and Order* (EB-2020-0030), December 17, 2020, p.10-11

No Need For The Account

Hydro One has not demonstrated that there is any need for the account.

Hydro One's evidence is that, without the ATP Account, it would either need to defer commencement of the qualifying project until it receives capital expenditure approval, or that it will have to re-prioritize projects included in approved revenue requirements.[17] SEC does not understand why this would be the case. The ATP Account only provides the potential for recovery of costs if a project is ultimately not built. If it is built, pre-construction costs are capitalized, and will be considered in the context of an initial rate application, either by a new partnership or by Hydro One itself.

Considering that the eligible projects are only those that the IESO says are needed or, the Minister through the OEB requires Hydro One to develop and construct, the risk of the projects not being built is small.

Hydro One has not pointed to another circumstance where the lack of a similar account has impacted its work on a similar type of project, or the execution of the rest of its approved transmission plan. The evidence would indicate otherwise.

Without a similar account in place, it developed, constructed, and transferred to a partnership both the Bruce-to-Milton Line and the Niagara Reinforcement Line Project.[18]

Moreover, Hydro One was previously willing to begin development work on the Lake Superior Link project, which was a highly speculative undertaking considering it was meant to compete against NextBridge's East-West Tie Line that the OEB had already designated.[19]

The best evidence that the lack of any deferral account has had no impact on Hydro One's operations is that for the two eligible projects that are not already covered by an existing deferral account, Hydro One has begun development work, and reached the point where all the costs are now capitalized.[20] With respect to one of those projects, Chatham SS to Lakeshore TS, the IESO requested Hydro One undertake development work more than 2 years ago. Hydro One did so without any complaint, and did not bring forward an application for a deferral account until this application.[21]

When asked directly about the driver of the proposed application, Hydro One did not point to the non-discretionary nature of these projects, but instead emphasized that Hydro One's intention is that the projects will eventually be transferred to a new partnership.[22] On that basis, it is unclear why the intention to transfer the projects requires a deferral account to protect Hydro One from the financial risk that these projects do not ultimately get constructed. While this may be a good reason for greater transparency and cost allocation, that does not require establishing a deferral account.

Hydro One also claims that another benefit of the ATP Account is for transparency purposes. SEC submits that, while the account may offer some transparency benefits if Hydro One brings a section 86 application to transfer ownership, it is not a reason for a deferral account.

[17] Interrogatory Response Staff #1(b),(c)
[18] See *Decision and Order* (EB-2017-0182/194/0364), December 20, 2018
[19] Interrogatory Response SEC 2(b)
[20] Interrogatory Response EP #10(a)(b)
[21] Application, Attachment B
[22] Interrogatory Response SEC 2(a)

Hydro One is a sophisticated entity that, in the regular course, segregates costs through its internal account systems for large projects. This is an accounting requirement in any case, and Hydro One and other utilities do this routinely. This should especially be the case if the expectation is the project will be transferred at some future point to a new entity. None of this requires OEB approval.

ATP Account Hides Full Picture of Hydro One Transmission Costs

SEC also believes there is a policy rationale for why the Board should deny this account. SEC is concerned that the effect of establishing the ATP Account may be to allow Hydro One to significantly understate its proposed spending in its transmission rate applications.[23] If the proposed ATP Account is approved, Hydro One will no longer include the cost of eligible projects in its transmission rate applications. The OEB and customers will not see the full picture of the company's transmission spending.

This is not a theoretical concern. In its Joint Rate Application evidence, Hydro One has presumed the OEB will approve the ATP Account, and so has not included the cost of any of these transmission projects in its forecast expenditures.[24]

From a customer's perspective, Hydro One transferring a project to a new entity is irrelevant from a rate impact perspective. Customers pay transmission rates based on the Uniform Transmission Rates ("UTR"), which aggregate all transmitters' approved revenue, including Hydro One and any affiliated new partnerships.

Understanding the full picture of Hydro One transmission costs is essential for the OEB and customers to properly consider potential tradeoffs, between spending for new transmission lines that projects such as those eligible, included in the ATP Account, and other areas of spending. Hydro One's proposal would mask these costs from a clear view as they are not included in its transmission rate applications. From a legal perspective, Hydro One may have an intention to transfer ownership of these constructed assets to a new partnership that may be created, However, until there is an approved section 86 application, they are projects of the company.

OEB Needs a Policy For One Asset Transmitters Rate Setting

Hydro One's acknowledgment that it expects all of its new large greenfield transmission line projects to be transferred and owned by separate new partnerships raises an issue of the appropriate rate-making treatment of these single asset transmitters. In this application, Hydro One identified three projects, and in its Joint Rate Application, it identified two more (the Longwood to Chatham, and Lakeshore to Leamington Transmission Lines).[25]

SEC strongly urges the OEB should consider, by way of policy consultation or otherwise, the proper rate-making approach, for any one asset entity before these assets go in service, and before these new entities file their initial rate applications.

As these types of arrangements increase, they present challenges for the rate-making approach which has generally been governed by the OEB's Handbook on Utility Rate Applications.[26] The incentive

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[23] Application, p.7-9; Interrogatory Response Staff #1, p.3

[24] See for example, EB-2021-0110, Exhibit B-2-1, Section 2.1, p.15, ft 13 where Hydro One explains that it has excluded costs for three projects identified in this application, as well as two additional investments on the basis that of its pending application for the ATP Account.

[25] EB-2021-0110Exhibit B-2-1, Section 2.8, p.3

[26] See [Handbook on Utility Rate Applications]

rate-making approaches, outlined in the Handbook, were designed for a utility such as Hydro One that has a growing rate base. They were not meant for a utility that owns a single asset whose rate base declines over time. Under the Handbook rate-making approaches, declining rate base from existing assets is offset by increasing rate base from new assets. With a single asset utility there is only one asset, and the effect of applying the Handbook is to build in rate increases where these transmitters will actually experience declining costs.

While some of this issue was recently canvassed in the context of NextBridge's Custom IR application[27], the OEB should consider the matter on a generic basis.

Summary

SEC submits that the OEB should deny approval of the proposed ATP Account. The appropriate time for the OEB to consider such an account is in the context of Hydro One's Joint Rate Application (EB-2021-0110), where the rate framework for 2023 to 2027 is to be determined.

All of which is respectfully submitted.

Yours very truly,
Shepherd Rubenstein P.C.

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Mark Rubenstein

cc: Ted Doherty, SEC (by email)
Applicant and intervenors (by email)

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[27] *Decision and Order* (EB-2020-0150), June 17, 2021