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BY EMAIL AND RESS

February 11, 2022

Ms. Nancy Marconi
Acting Registrar
Ontario Energy Board
Suite 2700, 2300 Yonge Street
P.O. Box 2319
Toronto, ON M4P 1E4

Dear Ms. Marconi,

EB-2021-0110 – Custom IR Application (2023-2027) for Hydro One Networks Inc. Transmission and Distribution – Evidence Update and Schedule

This letter is in response to Intervenor letters received on February 8 and 9 with respect to Hydro One's letter dated February 7, 2022 in which Hydro One formally requested that the settlement conference be postponed to allow Hydro One to make necessary material amendments to its Application and evidence to reflect the impact of inflation.

In addition to other aspects, this letter will address the two primary concerns of Intervenors being the scope of the amendments and the reasonableness of the schedule proposed by Hydro One in its February 7 letter.

Background

In March 2018, the Ontario Energy Board (OEB) directed Hydro One to file a joint rate application for its transmission and distribution businesses for the 2023 to 2027 period. Historically, Hydro One staggered its transmission and distribution applications, thus spreading the impact of an external factor like inflation rates across time and across two different businesses. The combined nature of the current joint application means that the entire business is exposed to external factors over a single rate period.

Given the expanded scope of the Application, Hydro One began preparing well in advance and throughout 2020, completing its investment plan in 2021 and filing its joint rate application on August 5, 2021. Because of the lag between filing and the January 1, 2023 effective date, the company applied an inflationary assumption to each year in the 2021 to 2027 period to all costs using Ontario CPI forecasts of 2.0% each year.

In recent months, the economy has experienced unprecedented levels of inflation that could not have been contemplated when the OEB required the Application to be made or at the time of filing. As noted

in Hydro One's February 7 letter, even inflation trends in the Fall of 2021 did not fully reflect inflationary impacts in 2022 that are now shown in the January 2022 projections and also in projections just released on February 10, 2022. Inflationary pressures are materializing throughout Hydro One's supply chain. Prices for copper, steel and aluminum prices have risen significantly. Ontario CPI rose 3.5% on an annual average basis in 2021. The January 2022 Consensus Forecast for Canadian CPI includes annual average inflation projections for 2022 which range from 2.6% to 4.5%, with a 3.4% mean. The February 2022 Consensus Forecast for Canadian CPI has an annual average inflation projection for 2022 ranging from 3.2% to 4.4%, with a 3.7% mean.

As noted in Hydro One's February 7 letter, the company will not be able to achieve the associated volumes of work included in the investment plan for 2023-2027, since the full inflationary impacts in 2021 and 2022 are not reflected in the 2023 forecast amounts. In other words, costs in 2023, for example, are based on costs in 2020 inflated by 2.0% into 2021, 2.0% into 2022 and 2.0% into 2023. To the extent inflation is higher in 2021 and 2022, costs in the Application for 2023 will be understated relative to the associated volumes of work. This impact will have a cumulative effect throughout the rate period, as forecast OM&A and capital expenditures will start from an inappropriate base amount in 2023.¹

As a result of inflationary pressures, the inflation assumption underpinning Hydro One's System Plans and OM&A forecast has materially changed. Hydro One, therefore, has the obligation to make an amendment, and intends to do so, to account for the above material change. Rule 11.02 of the OEB's *Rules of Practice and Procedure* requires Hydro One to file an amendment when it becomes aware of new information that constitutes a material change to the evidence.

With respect to the Settlement Conference, the timing of Hydro One receiving the revised Consensus Forecast in the latter part of January 2022 and the consideration of the implications for the Application thereafter unfortunately coincided with the timing of the Settlement Conference. In this regard, Hydro One notes that it is respectful of and takes very seriously its participation in the settlement process. As a result, given its obligation under the OEB Practice Direction on Settlements that a participant in a settlement conference once aware of a material change in its pre-filed evidence prior to a settlement conference must disclose that material change, Hydro One reached the difficult decision to postpone its participation in the Settlement Conference until its evidence was appropriately amended. Proceeding without the evidence amendment would not accurately reflect the cost to execute the work contemplated by Hydro One in its Application and would not enable meaningful settlement discussions between the parties.

1. Description of the Inflation Amendment

Hydro One applied inflationary assumptions of 2.0% per year to all costs in the plan from 2021 to 2027. With the material change in this assumed inflation rate, Hydro One will amend as follows:

- The 2021 inflationary assumption of 2.0% will be replaced with actual Ontario CPI of 3.5%

¹ For OM&A, understated costs in 2023 will persist in each subsequent year of the rate period, because OM&A costs are escalated in 2024-2027 by the prior year * (I-X). For capital, the impact of understating inflation assumptions in 2021 and 2022 will impact the capital for 2023-2027 as the 2023-2027 costs estimates are currently based on outdated inflation assumptions.

- The 2022 inflationary assumption of 2.0% will be replaced with a forecast Ontario CPI

By taking this approach, the work contemplated under Hydro One's Plans will be unchanged, but the costs will be adjusted to align with the forecast costs to execute the work based upon the same methodology (as noted below) as originally employed by Hydro One.

Intervenors, in their correspondence, have made various assertions as to what Hydro One's amendment should include and the degree of detail to be reflected in that amendment. However, it is Hydro One that has the obligation to amend its evidence and to do so in an appropriate manner. It is not for the Intervenors to stipulate especially at this stage the content or extent of the evidence which Hydro One will file and on which it will rely in support of its Application.

Hydro One is in the process of considering alternative approaches to the amendment (including recognizing the comments of various Intervenors) to show the impacts of inflation on the Application, while still complying with the requirements under the OEB's Rules of Practice and regulatory efficiency. Subject to pursuing an alternative approach, Hydro One's amendment will include, at a minimum, updates to capital costs, the associated in-service additions, and OM&A costs. In addition, Hydro One will update its rate base, revenue requirement and bill impacts. Hydro One appreciates Intervenors' desire to see the impacts at the project and program level. Hydro One notes that in the current evidence the forecast inflation rates of 2.0% per year were applied evenly to all costs in the investment plan, and all costs will be similarly adjusted for increased inflation rates. As such, the vast majority of projects and programs will not be materially impacted by the inflationary adjustment.² Nevertheless, Hydro One will provide an evidentiary update that reflects all material changes and clearly explains the mechanics of the inflationary adjustment. Hydro One will also provide revised interrogatories and undertakings that are materially impacted by the amendment. Contrary to the assertions made by Intervenors, Hydro One's evidence will not be a selective update. It will provide for material changes in a manner that enables the consideration of its Application in an effective and efficient manner.

2. Scheduling

In its letter of February 7, Hydro One proposed a revised schedule. This was done bearing in mind the overall objectives in Rule 2.01, including the objective of expediency and efficiency of the process, and bearing in mind the timelines previously established by the OEB in terms of the sequencing of the various steps in this Application. The proposed revised schedule was prepared in order to not unduly delay the timing of the remaining steps.

The first step in the proposed revised schedule is for Hydro One to file its amendment by March 14. Hydro One expects to be able to meet that timing.

The revised schedule also sets out proposed timing for subsequent steps including the revised timing for the settlement conference and the hearing in the event the Application is not settled or is partially settled. Intervenors have raised concerns as to whether the timing for the subsequent steps should be fixed at this point, before they have a chance to review the amendment.

² Using \$1 million threshold for Distribution and \$3 million threshold for transmission.

Hydro One is of the view that the proposed revised schedule is reasonable having regard to the nature of the intended update. Having said that, the specific timing of the steps after March 14 does not need to be fixed now if the OEB is more inclined to wait until the amendment is filed. The timetable for subsequent steps could be determined by the OEB at that point if that is preferable.

3. Bluepage Update

Some Intervenors again raised the topic of a bluepage update, seeking an overall update reflecting 2021 actuals. This is separate from Hydro One's intended inflation-related amendment.

The OEB previously ruled on the request for a bluepage update, and has repeatedly indicated that it is not required, as long as other appropriate evidence updates are provided during the other steps in the process. Hydro One has been doing so, by responding to OEB Staff and Intervenor interrogatories and undertaking requests for various updated information. The provision of year end 2021 actuals will not provide the Commission with materially different information relative to the Q3 2021 actuals provided during the course of interrogatories.

In Hydro One's view, and having regard to previous direction from the OEB, a bluepage update should still not be necessary for the same reasons the OEB has already indicated, and Hydro One is not requesting a bluepage update. Doing so would also further impact the schedule.

In the circumstances, we assume the OEB does not intend to revisit its decision on this point. However, if it were inclined to do so, Hydro One would need to receive the OEB's direction in this regard within days of this letter in order to provide a bluepage update by the end of April. A delay until the amendment is filed on March 14 will result in a corresponding period into to May.

4. Other Matters

Unrelated to the inflation amendment, Hydro One mentioned in its February 7 letter that it will be in a position to file a mechanistic update to its load forecast. Also, it gave an advanced heads up that it may seek to file brief reply evidence from Clearspring in response to the recently delivered PEG evidence. Intervenors raised some questions or concerns regarding these two points. Hydro One notes that these points are separate from the inflation-related amendment that was the focus of the February 7 letter and the focus of the proposed revised schedule.

In respect of the load forecast, Intervenors have indicated that they seek to understand the scope of the update. The IESO's CDM forecasts set out in its Annual Planning Outlook (APO) issued in December 2021 have changed materially relative to the IESO's 2020 APO. Based on Rule 11.02, if these forecast changes from the IESO result in a material change to Hydro One's load forecast, Hydro One is required to update its CDM forecast to reflect the IESO's latest CDM forecast.

In respect of the Clearspring reply evidence point, there is not yet any issue that requires the OEB's consideration or determination. As indicated in our February 7 letter, Hydro One is considering this point and will correspond further with the OEB on this in the event (and when) it seeks to file a reply report. On this issue, Hydro One will bear in mind the registrar's previous comments in Procedural Order No. 2. In that regard, we would note that – contrary to the suggestion by Intervenors that the OEB determined

Hydro One is not permitted to file reply – what the procedural order actually stated on this point (at page 14) was:

The OEB will not make provision for reply expert evidence from Hydro One at this time. The OEB may revisit this decision prior to the oral hearing if outstanding issues have not been addressed through the interrogatory process and the utilization of Rule 13A.04.

Accordingly, Hydro One will correspond further on this point as need be, and any issue could be addressed at that point.

As indicated in our February 7 letter, the intended mechanistic load forecast update, and any filing of Clearspring reply evidence, are not expected to impact the overall schedule or cause any additional delay.

Summary

Hydro One intends to amend its Application in accordance with its obligation under the rules and Practice Direction on Settlement Conference, and with a view to having an efficient process. It expects to be in a position to file the amendment by March 14. The filing of this amendment needs to be done at this stage, prior to the settlement conference, to allow for meaningful settlement discussions and an appropriate process going forward in the event the Application is not settled.

While Hydro One has suggested a timetable for subsequent steps after the filing of the amendment, and believes the proposed schedule of steps is reasonable, Hydro One understands if the preference is to wait until the amendment is filed in order to fix the rest of the timetable.

Sincerely,

A handwritten signature in cursive script that reads "Frank D'Andrea".

Frank D'Andrea