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BY EMAIL

November 1, 2022

Ms. Nancy Marconi
Registrar
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4
Registrar@oeb.ca

Dear Ms. Marconi:

**Re: Ontario Energy Board (OEB) Staff Submission on the Settlement Proposal
Hydro One Networks Inc.
2023-2027 Joint Transmission and Distribution Rate Application
OEB File Number: EB-2021-0110**

Please find attached OEB staff's submission on the settlement proposal in the above referenced proceeding, pursuant to Procedural Order No. 7.

Yours truly,

Martin Davies
Senior Advisor, Generation & Transmission

Encl.

cc: All parties in EB-2021-0110



ONTARIO ENERGY BOARD

OEB Staff Submission on Settlement Proposal

Hydro One Networks Inc.

2023-2027 Joint Transmission and Distribution Rate Application

EB-2021-0110

November 1, 2022

Background

Hydro One Networks Inc. (Hydro One) filed an application dated August 5, 2021 with the Ontario Energy Board (OEB) under section 78 of the *Ontario Energy Board Act, 1998*, seeking approval for changes to the rates that Hydro One charges for electricity transmission and distribution, beginning January 1, 2023 and for each following year through to December 31, 2027.

The OEB approved an Issues List in its January 13, 2022 Decision on Issues List and Procedural Order No. 3 (PO#3). The final approved Issues List is attached as Schedule A to PO#3.

A settlement conference was held between August 15, 2022 and August 24, 2022. Hydro One and the intervenors¹ participated in the settlement conference (collectively, the Parties).

Hydro One filed a settlement proposal on October 24, 2022 (the Settlement Proposal). All of the Parties supported the settlement proposal except the Canadian Union of Skilled Workers, Ice River Sustainable Solutions, the Power Workers' Union and the Society of United Professionals, which took no position on it.

The Settlement Proposal represents a comprehensive settlement on all issues set out in the Issues List.

General Comments on the Settlement Proposal

In accordance with Section 11 of the OEB's *Practice Direction on Settlement Conferences*, OEB staff's submission with the OEB will comment on two aspects of the Settlement Proposal: (1) whether the Settlement Proposal represents an acceptable outcome from a public interest perspective, and (2) whether the accompanying explanation and rationale is adequate to support the Settlement Proposal.

¹ Six approved intervenors in the proceeding did not participate in the Settlement Conference: ENWIN Utilities Ltd., Essex Powerlines Corporation, Independent Electricity System Operator (IESO), Richard Gruchala (Independent Participant), Ontario Power Generation Inc., and Ontario Federation of Agriculture.

OEB staff is of the view that the Parties have provided sufficient explanation in the settlement proposal as to why the agreed upon resolution is appropriate, including by citing the applicable sections of the evidence.

OEB staff would further note that as is typical for a large rate proceeding of this type, a number of stakeholders participated, representing a range of perspectives. As noted earlier, 18 different interest groups (many of which represent customers) took part in the settlement conference, including many of the most experienced OEB intervenors.

For these reasons, in this submission, OEB staff will examine the settlement proposal as a whole, rather than commenting on every aspect on an issue-by-issue basis.

The tables below, reproduced from the Settlement Proposal, provide information on the Custom Incentive Rate-setting (Custom IR) framework arising from the settlement proposal:

Table 1: Transmission Custom IR Framework

	Hydro One Proposal	Settlement Proposal
Term	5 years	5 years
Overall Structure	I-X+C	I-X+C
Inflation Factor (I)	Updated annually to reflect OEB issued factors for transmitters	Updated annually to reflect OEB issued factors for transmitters
Productivity Factor (X)	0%	0.15%
Capital Factor (C)	Updated annually for OEB inflation	Updated annually for OEB inflation
Supplemental Stretch on Capital	0.15%	0.20%
ESM	100 bps deadband 50/50 sharing Disposition of available balances in the next rebasing	100 bps deadband 50/50 sharing Disposition of 2021 to 2024 balances in annual update for 2026 rates
Capital In-Service Variance Account (CISVA)	Proposed	Agreed not to establish
Z-Factor	OEB-approved criteria	OEB-approved criteria

Table 2: Distribution Custom IR Framework

	Hydro One Proposal	Settlement Proposal
Term	5 years	5 years
Overall Structure	I-X+C	I-X+C
Inflation Factor (I)	Updated annually to reflect OEB issued factors for transmitters	Updated annually to reflect OEB issued factors for transmitters
Productivity Factor (X)	0.30%	0.45%
Capital Factor (C)	Updated annually for OEB inflation	Updated annually for OEB inflation
Supplemental Stretch on Capital	0.15%	0.20%
ESM	100 bps deadband 50/50 sharing Disposition of available balances in the next rebasing	100 bps deadband 50/50 sharing Disposition of 2021 to 2024 balances in annual update for 2026 rates
Capital In-Service Variance Account (CISVA)	Proposed	Agreed not to establish
Z-Factor	OEB-approved criteria	OEB-approved criteria

The shaded areas in the tables above indicate where changes in the Custom IR framework were negotiated during the settlement process. OEB staff notes that for both distribution and transmission business segments, the productivity factors and supplemental stretch factors have been increased, which will provide Hydro One with additional incentives to achieve greater efficiencies during the 2023 to 2027 period. In addition, any Earnings Sharing Mechanism (ESM) balances will be disposed for the 2021 to 2024 period as part of Hydro One's annual update application for 2026 rates, which is earlier than Hydro One had proposed in the application as filed. OEB staff views both these changes as beneficial to Hydro One's customers since the ESM is asymmetrical in the favour of customers. OEB staff considers the resulting settlement of the Custom IR frameworks as being in the public interest.

In the tables that follow, OEB staff provides a summary of the impacts of the Settlement Proposal on Hydro One's capital expenditures and rate base relative to what had been proposed in the application:²

² Note that in these tables and the ones that follow, there may be some minor rounding differences between the numbers in the tables and those appearing in the Settlement Proposal. The values set out below are prepared for this staff summary for illustrative purposes only, and do not represent a modification to the values shown in the Settlement Proposal.

Table 3 - 2023 to 2027 Settled Capital Reductions (\$M)						
	2023	2024	2025	2026	2027	Total
Proposed Transmission	1,509.30	1,540.70	1,526.60	1,538.50	1,524.30	7,639.40
Settled Transmission	1,362.10	1,389.40	1,373.30	1,382.10	1,370.20	6,877.00
Reduction Due to Settlement	147.20	151.30	153.30	156.40	154.10	762.30
Proposed Distribution	1,057.90	1,081.90	1,179.70	1,127.90	1,127.20	5,574.50
Settled Distribution	920.80	949.20	1,040.00	992.50	991.30	4,893.80
Reduction Due to Settlement	137.10	132.70	139.70	135.40	135.90	680.80
Proposed Total	2,567.20	2,622.60	2,706.30	2,666.40	2,651.50	13,213.90
Settled Total	2,282.90	2,338.60	2,413.30	2,374.60	2,361.50	11,770.80
Reduction Due to Settlement	284.30	284.00	293.00	291.80	290.00	1,443.10
Settlement Reduction (%)	11.1	10.8	10.8	10.9	10.9	10.9

Table 4 - 2023 to 2027 Settled Rate Base Reductions (\$M)						
	2023	2024	2025	2026	2027	Average
Proposed Transmission	14,611.50	15,516.60	16,585.50	17,602.60	18,534.10	16,570.06
Settled Transmission	14,534.40	15,342.40	16,271.00	17,148.50	17,940.20	16,247.30
Reduction Due to Settlement	77.10	174.20	314.50	454.10	593.90	322.76
Proposed Distribution	9,394.70	10,031.40	10,764.20	11,477.90	12,104.70	10,754.58
Settled Distribution	9,460.00	9,979.00	10,572.50	11,152.60	11,655.70	10,563.96
Reduction Due to Settlement	-65.30	52.40	191.70	325.30	449.00	190.62
Proposed Total	24,006.20	25,548.00	27,349.70	29,080.50	30,638.80	27,324.64
Settled Total	23,994.40	25,321.40	26,843.50	28,301.10	29,595.90	26,811.26
Reduction Due to Settlement	11.80	226.60	506.20	779.40	1,042.90	513.38

Table 5 - 2023 to 2027 Settled In-Service Additions Reductions (\$M)						
	2023	2024	2025	2026	2027	Total
Proposed Transmission	1,404.50	1,393.20	1,795.60	1,347.50	1,683.80	7,624.50
Settled Transmission	1,334.10	1,264.20	1,631.80	1,212.70	1,512.50	6,955.20
Reduction Due to Settlement	70.40	129.00	163.80	134.80	171.30	669.30
Proposed Distribution	1,012.50	1,080.90	1,266.60	1,116.90	1,165.90	5,642.90
Settled Distribution	910.00	947.40	1,113.10	984.60	1,022.60	4,977.80
Reduction Due to Settlement	102.50	133.50	153.50	132.30	143.30	665.10
Proposed Total	2,417.00	2,474.10	3,062.20	2,464.40	2,849.70	13,267.40
Settled Total	2,244.10	2,211.60	2,744.90	2,197.30	2,535.10	11,933.00
Reduction Due to Settlement	172.90	262.50	317.30	267.10	314.60	1,334.40
Settlement Reduction (%)	7.2	10.6	10.4	10.8	11.0	10.1

Tables 3 to 5³ above show that capital expenditure reductions arising from the Settlement Proposal are in the 11 percent range. OEB staff notes that this level of reduction compares to reductions in the 8 to 10 percent range that were ordered by the OEB in the most recent cost-based Hydro One Transmission (Transmission) and Hydro One Distribution (Distribution) decisions.⁴ The reductions in capital in-service additions are also in a similar range. OEB staff considers these proposed adjustments as reasonable.

³ Tables 3 to 5 consolidate information from various sections of the EB-2021-0110 *Settlement Proposal*, October 24, 2022 (Settlement Proposal): Table 3 from Settlement Proposal Tables 22 and 25, Table 4 from Settlement Proposal Tables 21 and 24, and Table 5 from Settlement Proposal Tables 23 and 26.

⁴ For Transmission: EB-2019-0082 Hydro One Networks Inc. *Decision and Order*, April 23, 2020, p. 3 – reduction of 10.4% and for Distribution: EB-2017-0049 Hydro One Networks Inc. *Decision and Order*, March 7, 2019, pp. 2-3 - reduction of 8.4%.

Table 6- 2023 Settled Total OM&A Expenses (\$M)		
Proposed Transmission		450.2
Settled Transmission		433.7
Reduction Due to Settlement		16.5
Proposed Distribution		634.4
Settled Distribution		616.3
Reduction Due to Settlement		18.1
Proposed Total		1084.6
Settled Total		1050
Reduction Due to Settlement		34.6
Settlement Reduction (%)		3.2

Table 6⁵ above shows that operation, maintenance, and administrative (OM&A) expense reductions arising from the settlement proposal are in the three percent range. OEB staff notes that this level of reduction compares to a reduction of 2.7%⁶ that was ordered by the OEB in the most recent cost-based Transmission decision and 5.6%⁷ in the most recent cost-based Distribution decision. OEB staff notes that this 5.6% reduction included \$17 million related to Hydro One's pension plan surplus at that time. In the absence of this amount, the overall reduction would have been around 2.7%. OEB staff considers these proposed adjustments as reasonable.

OEB staff further notes that the combined effect of these reductions is a significant reduction in the revenue requirement required to be collected from customers in the five-year period from 2023 to 2027, particularly in the latter part of the rate term, as shown in Table 7⁸ below:

⁵ Consolidation of Settlement Proposal, Tables 27 and 28.

⁶ *Decision and Order*, April 23, 2020, p.3.

⁷ *Decision and Order*, March 7, 2019, p.94.

⁸ Consolidation of Settlement Proposal, Tables 17 and 20.

Table 7 - 2023 to 2027 Settled Revenue Requirement Reductions (\$M)						
	2023	2024	2025	2026	2027	Total
Proposed Transmission	1,849.30	1,968.20	2,063.00	2,182.50	2,266.60	
Settled Transmission	1,831.90	1,938.10	2,017.60	2,111.20	2,180.90	
Reduction Due to Settlement	17.40	30.10	45.40	71.30	85.70	249.90
Proposed Distribution	1,669.10	1,753.30	1,832.20	1,934.80	2,024.60	
Settled Distribution	1,654.60	1,727.30	1,786.50	1,870.40	1,942.80	
Reduction Due to Settlement	14.50	26.00	45.70	64.40	81.80	232.40
Proposed Total	3,518.40	3,721.50	3,895.20	4,117.30	4,291.20	19,543.60
Settled Total	3,486.50	3,665.40	3,804.10	3,981.60	4,123.70	19,061.30
Reduction Due to Settlement	31.90	56.10	91.10	135.70	167.50	482.30
Settlement Reduction (%)	0.9	1.5	2.3	3.3	3.9	2.5

The impacts included in the Settlement Proposal result in a total of \$482.3 million in savings for Hydro One's customers as a result of negotiated reductions in Hydro One's revenue requirements over the 2023 to 2027 period, or an average annual 2.5% reduction.⁹ OEB staff considers these reductions as reasonable and beneficial to Hydro One's customers and, as such, in the public interest. OEB staff also notes that these reductions do not reflect any impacts arising from changes to the load forecasts that are discussed further below.

Table 8 below provides the impacts of the Settlement Proposal on the Transmission and Distribution load forecasts:¹⁰

Table 8 - Load Forecast 2023 to 2027					
	2023	2024	2025	2026	2027
Proposed Transmission*	19,416	19,414	19,303	19,191	19,238
Settled Transmission	19,600	19,650	19,402	19,321	19,392
Increase Due to Settlement	184	236	99	130	154
Proposed Distribution**	35,522	35,497	35,400	35,273	35,379
Settled Distribution	35,902	35,998	35,608	35,540	35,701
Increase Due to Settlement	380	501	208	267	322

* 12-Month Average Peak in MW

** GWh Delivered Forecast

OEB staff notes that the settled load forecasts are higher than those which were

⁹ Consolidation of Settlement Proposal, Tables 2 and 5

¹⁰ Consolidation of Settlement Proposal, Tables 7 and 8

proposed, which will provide additional benefits to customers and are, as such, also in the public interest. These adjustments arise from a modification to the methodologies used by Hydro One to determine its Transmission and Distribution load forecasts that is incorporated into the Settlement Proposal. The agreement among the Parties is that Hydro One is to modify the initially proposed load forecasts by reducing the assumptions for incremental achievable potential conservation and demand management (CDM) impacts by 100% for each of 2023 and 2024, and by 35% for each of the years from 2025 to 2027.

While OEB staff supports the settlement of this matter outlined above, given the specific circumstances of this proceeding, OEB staff also notes that, on October 4, 2022, the Ministry of Energy provided a new directive to the IESO that will expand the budget for the current provincial CDM framework, which is expected to lead to additional energy savings from CDM. As such, OEB staff would not see this settlement as setting a precedent for future proceedings.

OEB staff further notes a couple of significant aspects of the Settlement Proposal as related to deferral and variance accounts. First, disposition of the net credit balance for the Transmission deferral and variance accounts will take place over a one-year period in 2023, rather than over a five-year period as proposed, and second, disposition of the net credit balance for the Distribution deferral and variance accounts will take place over a three-year period, from 2023 to 2025, rather than over a five-year period as initially proposed. These changes will provide another positive benefit to customers, particularly in the near term, arising from this Settlement Proposal.

The table below¹¹ shows the impact of the Settlement Proposal on the percentage rate increases (or decreases), based on typical consumption levels for residential and general service classes¹²:

¹¹ Reproduced from Settlement Proposal, Table 10.

¹² Typical Residential Medium Density (R1) customer excluding the impact of the Distribution Rate Protection (DRP) program with monthly consumption of 750 kWh and a typical General Service <50kW (Gse) customer at the 2,000 kWh/month consumption level.

Table 9 - Total Bill Impacts - Changes in Transmission and Distribution Revenue Requirements and DVA Dispositions (%)

	R1 (w/o) DRP 750 kWh	Gse 2,000 kWh
2023 - As Applied For	-1.2	-1.5
- Settled	-1.2	-1.6
2024 - As Applied For	1.6	0.9
- Settled	1.2	0.6
2025 - As Applied For	2.3	2.1
- Settled	1.9	1.8
2026 - As Applied For	2.6	2.7
- Settled	2.8	2.6
2027 - As Applied For	2.2	2.1
- Settled	1.8	1.7
5 yr avg - Applied For	1.5	1.3
- Settled	1.3	1.0

OEB staff notes that the changes in the above table are well below the 10% mitigation level in all cases, even prior to the reductions negotiated as part of the settlement process. The effect of the acceptance of this Settlement Proposal by the OEB will be to further reduce these impacts, which will represent a benefit to Hydro One's customers.

Additional Comments on Certain Specific Aspects of the Settlement Proposal

As noted above, OEB staff has examined the Settlement Proposal as a whole and has therefore focused this submission on providing high-level contextual observations. There are, however, a number of aspects of the Settlement Proposal where some additional comments may be of assistance to the OEB.

First, the Settlement Proposal contains a number of specific commitments by Hydro One that will advance planning to deal with critical issues, particularly climate change on a going-forward basis. These include a commitment by Hydro One to include, in future operational and capital investment plans, a discussion of how the proposed spending will directly support the achievement of Hydro One's climate change policy commitments by 2030 and 2050.

Specifically, Hydro One has made commitments to: (1) provide long-term capital plan information, (2) provide a study to be prepared by an independent consultant to examine general electrification scenarios for the 2030-2050 timeframe, (3) develop and

implement a robust planning process that appropriately considers non-wires solutions, including CDM, to meet system service needs, and (4) meaningfully consider the goals of municipal energy and emission plans with a view to pursuing cost efficiencies, reduced emissions, and enhanced energy outcomes for consumers in Ontario served by Hydro One.

Second, OEB staff notes that on March 31, 2022, Hydro One filed an evidence update to reflect the impact of inflation on its investment plans. This resulted in planned OM&A costs in 2023 and capital costs for 2023 to 2027 increasing to reflect current higher inflation levels up to 2023 with the expectation of inflation returning to normal levels (two percent) over the 2024 to 2027 rate period.

However, Hydro One had additionally proposed to further update its inflation assumptions for 2022 and 2023 at the time of the draft rate order process to reflect the most recent inflation actuals and forecast then available, up to a cap of 10% cumulative inflation over 2022 and 2023. The Settlement Proposal changes this originally proposed approach to eliminate any further updates by Hydro One as part of the current application to reflect changes to inflation for 2022 and 2023. This will provide Hydro One's customers with greater certainty as to the potential impacts of inflation on their bills.

Additionally, the Settlement Proposal contains agreement that both Hydro One's Transmission System Plan and Distribution System Plan sufficiently address the unique rights and concerns of Indigenous customers and rights-holders. Furthermore, the Parties have also agreed that Hydro One Distribution will undertake competitive procurement processes for reliability services from energy storage solutions for projects over the 2025-2027 period and when doing so will actively seek economic participation or equity investment opportunities from First Nations as part of its standard procurement practice. These agreements provide benefits to Indigenous customers and rights-holders and are, in OEB staff's view, in the public interest.

As well, OEB staff notes that there a number of income tax-related matters agreed to in the Settlement Proposal, particularly as they relate to deferral and variance accounts, including: (1) that the amounts pertaining to accelerated capital cost allowance benefits captured in existing variance accounts are to be calculated based on actual capital additions, as opposed to forecast additions (as originally proposed), (2) the establishment of a new account to capture the clean energy tax credits contemplated in the 2022 Federal Budget issued on April 7, 2022,¹³ and (3) the establishment of an account to facilitate Hydro One's updated approach to tax-deductible capitalized

¹³ <https://budget.gc.ca/2022/home-accueil-en.html>

overhead costs.¹⁴ Each of the above applies to both the Transmission and Distribution businesses, and in OEB staff's opinion, represent substantive potential benefits to ratepayers, by way of flowing various income tax benefits to them through rates.

OEB staff also notes that the Parties have agreed that, subject to the accounting system limitations identified by Hydro One during this proceeding and the issuance by the International Accounting Standards Board of a final set of standards pertaining to rate-regulated activities, Hydro One will provide in its next cost-based rate application, on a best efforts basis, estimated impacts of an initial transition from US Generally Accepted Accounting Principles (US GAAP) to International Financial Reporting Standards (IFRS) for regulatory purposes, as at the beginning of the next rate term, as well as estimated impacts on the annual revenue requirements for the remainder of the rate term. This will, in OEB staff's view, provide the OEB with the necessary information to consider the benefits of increased comparability between Hydro One's financial records to other utilities in Ontario (and Canada more broadly), the majority of which currently report their financial results under IFRS. This will also allow the OEB to evaluate the potential benefits of greater alignment amongst all utilities in the sector with respect to their ratemaking treatment.

Finally, OEB staff highlights that there are two new deferral and variance accounts included in the Settlement Proposal for the Distribution segment related to energy storage: one pertaining to grid-scale storage and another to behind-the-meter residential storage programs. With respect to the grid-scale storage account, if Hydro One enters into an arrangement with a third-party to provide reliability services, the account captures the difference between Hydro One's current accounting treatment of the forecast costs for a grid scale energy storage project, and any alternative accounting treatment informed by any future OEB guidance pertaining to cost recovery for innovative solutions. The residential storage account would record the net revenue to Hydro One Distribution, where a third-party is contracted to aggregate Hydro One owned residential battery storage units, for the purposes of participating in the IESO markets, and generates net revenues to the benefit of Hydro One Distribution – in a manner consistent with the outcome of the OEB's Framework for Energy Innovation consultation.¹⁵

In OEB staff's opinion, these accounts effectively serve to allow for Hydro One to propose innovative solutions in its system plans, including potential third-party

¹⁴ Under Hydro One's updated approach, for tax purposes, capitalized overhead costs are deducted immediately on the basis that they are not directly related to the acquisition or construction of capital assets and are considered recurring costs incurred as part of the day-to-day expenses of operating the business

¹⁵ EB-2021-0118

arrangements associated with those solutions, while also ensuring that these proposals do not supersede or presuppose the outcomes of the OEB's ongoing Framework for Energy Innovation consultation.

Conclusion

OEB staff concludes based on the preceding discussion that: (1) the Settlement Proposal represents an acceptable outcome from a public interest perspective, and (2) the accompanying explanation and rationale is adequate to support the Settlement Proposal.

~All of which is respectfully submitted~