Hydro One Networks Inc.
483 Bay Street
7th Floor South Tower
Toronto, Ontario M5G 2P5
HydroOne.com

Joanne Richardson
Director, Major Projects and
Partnerships
C 416.902.4326
Joanne.Richardson@HydroOne.com

BY EMAIL AND RESS

February 29, 2024

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

Dear Ms. Marconi,

EB-2023-0188 – Evaluation of Policy on Utility Consolidations - Hydro One Networks Inc. Comments

On February 8, 2024, the Ontario Energy Board issued the OEB Staff Discussion Paper on Evaluation of Policy on Utility Consolidations. Hydro One hereby submits its comments on the discussion paper.

An electronic copy of the comments has been submitted using the Board's Regulatory Electronic Submission System.

Sincerely,

Joanne Richardson

1.0 INTRODUCTION

Hydro One Limited, through its wholly owned subsidiaries, is Ontario's largest electricity transmission and distribution provider with approximately 1.5 million valued customers, approximately $32.8 billion in assets as of December 31, 2023, and annual revenues in 2023 of approximately $7.8 billion.

Our team of approximately 9,700 skilled and dedicated employees proudly build and maintain a safe and reliable electricity system which is essential to supporting strong and successful communities. In 2022, Hydro One invested approximately $2.5 billion in its transmission and distribution networks and supported the economy through buying approximately $2.5 billion of goods and services.

We are committed to the communities where we live and work through community investment, sustainability, and diversity initiatives. We are designated as a Sustainable Electricity Leader™ by Electricity Canada. Hydro One Limited's common shares are listed on the TSX and certain of Hydro One Inc.'s medium term notes are listed on the NYSE.

1.1 SUMMARY OF KEY FEEDBACK

Since the establishment of the no harm test, Hydro One has participated in OEB proceedings related to the acquisition and integration of various utilities over the last two decades. Hydro One has been a leader and active participant in achieving the aims of the province with respect to electricity distribution sector consolidation.

The comments provided herein on this OEB consultation are intended to assist with continuing to promote and incent distribution sector consolidation. Through these amendments Hydro One aims to establish consistent regulatory treatment across all MAAD applications, improve regulatory efficiency, as well as balance encouraging consolidation with responding to the Auditor General’s comments on same.[1] Hydro One has been cognizant to keep these aims in mind as it provides these comments.

[1] Office of the Auditor General of Ontario - Value-for-Money Audit: Ontario Energy Board: Electricity Oversight and Consumer Protection – November 2022

Hydro One commends OEB staff on the Evaluation of Policy on Utility Consolidations Discussion Paper (Discussion Paper). Hydro One agrees with OEB Staff that an overhaul of the OEB MAAD Handbook is unwarranted. Hydro One continues to believe that utility consolidation has been an effective tool for driving cost efficiencies within the sector and offers the following key recommendations for consideration which are discussed in further detail in the submission.

- Support for the continued use of the “no harm” test, with a request for further clarity in certain respects.
- Support for the use of revenue requirement over rate impacts as basis for the OEB’s “no harm” test.
- Recommendations for new language to support a more effective “no harm” test based on an improved, forward-looking assessment of the status quo, and the basis for why that it is essential to do so.
- Recommendations to improve the presentation of revenue requirement.
- Recommendations on the deferred rebasing period in specific scenarios involving multiple transactions.
- Recommendations to more precisely scope post-consolidation reporting to minimize incremental regulatory burden.
- Concerns with respect to Staff’s recommendations on post-consolidation performance metric reporting, and specifically metrics that are the subject of ongoing policy consultation on which utilities have expressed specific concerns or that conflict with prior OEB jurisprudence.
- Support for Staff’s proposals regarding Earning Sharing Mechanisms
- Other targeted or issue-specific feedback, as detailed below.

2.0 NO HARM TEST

<u>Hydro One supports the continuation of the “no harm” test</u> as the standard by which the OEB assesses proposed consolidations and agrees with OEB Staff that the updated version of the MAADs Handbook resulting from this consultative process should reflect the OEB’s current statutory objectives.

Hydro One appreciates the revisions OEB Staff has proposed in the Discussion Paper with respect to clarifications to the no harm test to encapsulate that both quantitative and qualitative information should be weighed in consideration of whether the proposed transaction, on a net basis, has a positive or neutral effect on the attainment of the OEB's objectives.

Hydro One's concerns with the language documented in the Discussion Paper regarding the no harm test are predicated on how the no harm test will be utilized, specifically, with respect to cost structures and what the transactions will be measured against. Hydro One supports the continued use of the no harm test but submits that additional clarity on what the no harm test will be measured against, i.e., the status quo requires further definition and/or clarity to avoid frustrating consolidation efforts during future MAADs and subsequent revenue requirement hearings. Hydro One's comments on this matter are provided in the following section on cost structures.

3.0 COST STRUCTURES & FUTURE RATE STRUCTURES

<u>Hydro One agrees with OEB Staff that revenue requirement provides a better depiction of the cost to serve ratepayers</u>, including impacts from depreciation, debt, tax rates, etc., to assess whether a transaction may introduce harm to ratepayers.

When assessing no harm, the OEB should take a holistic approach to distribution sector costs (e.g., how is the revenue requirement to run Ontario's distribution system in its entirety affected by the proposed transaction?). Hydro One submits that using this comprehensive approach will ensure that the issue of cost structures and rates are not conflated.

Hydro One appreciates that the Discussion Paper recognizes and acknowledges the unprecedented times ahead for the electricity sector. OEB Staff specifically document the emerging challenges faced within the energy sector posed by electrification and the energy transition driven by decarbonization targets, challenges related to cybersecurity, grid resiliency in the face of climate change, clean generation sources, management of distributed energy resources, and other changes as the energy sector evolves. Compounding these unprecedented expenditures is the fact that some utilities may not have made adequate investments in their distribution system to maintain their existing levels of service quality into the future.

Hydro One's main recommendation in this consultation will be that the OEB consider establishing a more reasonable "status quo".

To this end, <u>Hydro One recommends that the following language be added to the OEB MAAD's Handbook:</u>

> <u>In assessing harm, the OEB will be informed by a forward-looking assessment of the status quo. Applicants should not unreasonably rely on past results as a predictor of the future. Past results should not underpin the starting point of establishing whether a transaction will introduce harm in the future.</u>

Hydro One's recommendation is predicated on the following:

A. The OEB is a forward-looking regulator

Utilities that have been subject to an acquisition or merger have often not been rebased for many years prior to the acquisition.[2] Hydro One agrees that the budget values requested in the Revenue Requirement table shown on page 17 of the Discussion Paper are the appropriate starting point to view future revenue requirement forecasts versus commencing at a historic approved revenue requirement. A revised revenue requirement based on budget numbers provides a current view of where utilities are, and where the acquired entity is expected to be in the future. The use of their OEB-approved revenue requirement is not necessarily indicative of the current cost to serve the customers of the existing utility in a status-quo state on a go-forward basis.

The assessment of no harm must be congruent with the premise that the OEB is not a retro-active regulator. Thus, an assessment of harm must be forward looking and predicated on the needs of the industry and customers over the subsequent ten years following the transaction. The OEB has a duty to maintain and balance both i) the financial

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[2] For example, in EB-2018-0270, Hydro One highlighted that Orillia Power Distribution Corporation last rebased in 2010, effectively 8 years prior to the filing of the MAAD application.

viability of the electricity industry and ii) protect the interest of consumers. The continued operation of a utility well-beyond the up to ten-year timeframe being assessed in a MAAD is imperative, therefore, the cost structures being compared must represent the costs of the necessary investments required of the utility today and onwards.[3]

B. The OEB RRR results are unaudited

Reporting and record-keeping requirements (RRR) data underpins LDC efficiency cohorts, reliability, and quality of service data, as well as other items that have been frequently utilized for the purposes of establishing the status quo in OEB MAAD applications. As documented by the Pacific Economics Group (PEG) in their most recent report to the Board on benchmarking, "the source of the cost and output data used in the calculations is from the distributors as reported in the [RRR] filings. The study assumes that the data as reported by the distributors conforms to accounting policies and procedures described in the Accounting Procedures Handbook for Electricity Distributors that includes the Uniform System of Accounts and other instructions contained within the RRR filing system. It also assumes that the LDCs have taken ownership of the data provided to the OEB and significant revisions are not anticipated".[4] Similarly, when the OEB released the Report of the Board on Performance Measurement for Electricity Distributors: A Scorecard Approach outlined that while the OEB will create consistent Scorecard reports for distributors, ownership of the data and Scorecard resides with the distributor.[5]

The PEG model relies on the RRR data to provide a stretch factor where utilities with larger negative differences between actual and predicted costs are considered to be better

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[3] In EB-2016-0050, Hydro One's application to acquire Great Lakes Power Transmission Inc. (GLPT), the OEB denied the request to reset GLPT's revenue requirement. Therein, notwithstanding evidence from GLPT that the existing rates do not reflect current costs to serve, the OEB clarified that "rate-setting policies associated with consolidation are predicated on the notion that the going-in rates are the rates intended to provide the revenues required as the starting point to achieve savings over the deferred rebasing period". Existing rates therefore do not necessarily equate with the current revenue requirement and most certainly with the future revenue requirement of the status quo utility.

[4] Pacific Economics Group Research LLC - Empirical Research in Support of Incentive Rate-Setting: 2022 Benchmarking Update Report to the Ontario Energy Board – July 2023 – p.4

[5] EB-2010-0379 – Report of the Board: Performance Measurement for Electricity Distributors: A Scorecard Approach – March 5, 2014 – p.33

cost performers and therefore eligible for lower stretch factors.[6] The PEG model has been used by external bodies to assess the benefits of consolidation, notably a recent Auditor General Report questioned the benefits of consolidation and opined that small utilities appear more efficient than larger utilities[7] and thus questioned whether consolidations translate to reduced electricity rates or improved efficiency.

Inherently accepting RRR data without scrutiny ineffectively reflects the benefits of consolidation. If this data is going to continue to be utilized in this manner it is imperative that the OEB audit the results attested to by individual utilities on a more frequent basis.

Illustratively, Hydro One has recently filed an application to acquire the existing assets of Chapleau Public Utilities Corporation (CPUC).[8] This acquisition proposal is on the heels of a May 9, 2023, request by CPUC for Hydro One to receive an interim license to operate CPUC assets on behalf of CPUC. That relief was subsequently granted by the OEB given a multitude of operational, financial, and asset challenges described by the Mayor of Chapleau and the Board Chair of CPUC.[9] In providing the interim license relief, the OEB determined that CPUC was likely to fail to meet its obligations relating to the supply of electricity to consumers in the Township of Chapleau.[10] After having had an opportunity to review the existing condition of the assets of CPUC, Hydro One has highlighted significant concerns with the station assets and submarine cables of the utility and noted that there may need to be several transformer replacements based on the discovery of PCB oil.[11][12]

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[6] The model can make a prediction of each distributor's cost given its business conditions by multiplying the company's business condition variables by the model parameters and summing the results. The distributor's actual cost is then compared to that predicted by the model. The percentage difference between actual and predicted cost is the measure of cost performance. Companies with larger negative differences between actual and predicted costs are considered to be better cost performers and therefore eligible for lower stretch factors – ibid.
[7] Value-for-Money Audit: Ontario Energy Board: Electricity Oversight and Consumer Protection – Office of the Auditor General – November 2022 – pp. 44-45
[8] EB-2023-0328
[9] EB-2023-0144 - CPUC & Hydro One Request for s.59 Order – May 9, 2023 – p.2
[10] EB-2023-0144 – OEB Decision & Order – May 23, 2023 – p.2
[11] EB-2023-0144 – Hydro One Observation Report – September 29, 2023 – p.1
[12] This Observation Report also reflects why historical cost structures should not be relied upon as the starting point for establishing future cost structures.

Notwithstanding these facts, according to the PEG model, CPUC was rewarded for their cost performance and improved their cohort ranking by one cohort on July 18, 2023.[13]

Company Name	2021 Stretch Factor Ranking	2022 Stretch Factor Ranking
Chapleau Public Utilities Corp.	Cohort IV (0.45)	Cohort III (0.30)

Failure to sustain operations is not cost-effective and, absent Hydro One's intervention, had CPUC continued to operate "status-quo", existing customers of CPUC would likely have been exposed to the harm as expressed in the OEB's interim license determinations.

The CPUC example attests to the limitations of accepting this data without scrutiny.

C. Distribution System Plans (DSP) Inform Rate Setting but are Not OEB-Approved

DSPs are required by the OEB as a planning tool to demonstrate that the resulting investment plan is based on solid principles of prioritization and optimization. The OEB uses DSPs to inform the rate-setting process of the proposed investment plan. However, the OEB has also recognized in previous decisions[14] that the value of predecessor utilities' DSPs will have diminished long before any 10-year deferral period has ended. The forecasts that therefore underpin the status quo have little value for future rebasing applications as established by jurisprudence.

D. Acquiror's have limited line of sight to the status quo forecast

Inherently, in any commercial transaction, there is a risk to the acquiror of the divestor not providing goods or services in a condition expected by the acquiror. OEB Staff highlight in the Discussion Paper that consolidation applications, by their very nature, are based on best available forecasts at the time[15] and note that comments from some utilities of their concern included inheriting a utility that may need a significant capital and operating cost

[13] EB-2010-0379 - Incentive Rate Setting: 2022 Benchmarking Update for Determination of 2023 Stretch Factor Rankings – July 18, 2023 – p.2
[14] EB-2019-0018 – Alectra Utilities Corporation Application for Rates and Other Charges to Be Effective January 1, 2020 – OEB Partial Decision and Order – Issued January 30, 2020 – pp. 22-23
[15] Staff Discussion Paper, p. 14

infusion to be able to cope with increasing technological requirements and challenges.[16] The Staff Discussion Paper falls short, however, of identifying the fact that significant capital costs may also be necessary to simply bring an acquired utility up to current utility standards. This can happen for a multitude of reasons including utility risk tolerances, utility financial and/or operational capacity constraints or choosing to minimize or defer rate payer impacts.

A divestor, however, will not shine a bright light on these shortcomings in a commercial transaction as it would be a detriment to their negotiations. An acquiror that is competitively seeking to secure ownership of the utility would need to unearth this information in due diligence by reviewing unaudited RRR data, data room information made available by the divesting utility, and limited field inspections. From there, the acquiror will postulate how it can run the utility and estimate savings, accordingly. However, there is no definite way for an acquiror to validate their assumptions or the status quo forecast of the divesting utility, until the transaction is completed, and they have begun to operate the utility. Hydro One is also mindful that even a distributor who is not forecasting material growth in their service territory may not be able to meet the future needs of those customers, even if they maintain their business-as-usual operating model. *To operate the utility of the future will require something far beyond the premise that the past is an appropriate indicator of the future.*

To this end, Hydro One respectfully submits that simple extrapolations of a current utility's cost structures, inflated by OEB-approved inflation and or average utility rebasing increases (every 5 years) is not going to be an appropriate indicator of the true level of investment needs a distributor may require. The challenge exists that not being able to 'try before you buy' means that the true condition of acquired distribution assets and businesses is an ever-increasing risk that must use new methodologies for consideration of what the status quo would look like for a period up to ten years, a significant period for any business.

[16] Staff Discussion Paper, p. 10

Having the acquiror defend the validity and integrity of the status quo forecast by a then non-existent utility in a future rebasing application is unreasonable and without merit. There is no guarantee or unquestionable rigor behind how the status-quo was established. The risk, therefore, of both the forecast savings and the "status-quo" is entirely transferred to the acquiror despite the acquiror having no hand in establishing that status quo forecast, nor an appropriate opportunity to explore the condition and status of the target's distribution system assets and their expected future adequacy of service.

3.1 EXAMPLE REVENUE REQUIREMENT REQUIRES REFINEMENT

Hydro One appreciates that OEB Staff have provided some guidance on how revenue requirements will be displayed in future MAAD applications under both status quo and post-consolidation. Hydro One recommends that the filing requirements detail the other components of the revenue requirement calculation, such as shown below:

Rate Base
PP&E NBV
Working Capital Allowance
Closing Rate Base
Average Rate Base
OM&A
Depreciation
Tax
Cost of Capital
Cost of Debt
Cost of Equity
Total Cost of Capital
Revenue Requirement

4.0 DEFERRED REBASING PERIOD – MULTIPLE TRANSACTION

Hydro One believes that further guidance is needed for multiple consolidation transactions to not discourage consolidations. Hydro One acknowledges that the Staff Discussion Paper includes added information on multiple transaction consolidations but appears to be focused on situations where an already consolidated utility acquires an additional utility (e.g., the Alectra and Guelph Hydro example provided). A situation may also arise, where there's an existing utility currently in a deferred rebasing period and is subsequently purchased by another utility.

Besides requesting inclusion of some standard information (e.g., confirmation of deferral period timelines, timing of rebasing) there is little guidance provided on what deferral period applicants can expect. Staff's recommendation to address this issue on a case-by-case basis is not helpful and may deter future consolidations. Failure to provide clear guidance on how these situations will be addressed by the regulator could:

- Provide uncertainty in negotiating acquisitions. The deferral period directly impacts the purchase price an acquiring company can pay for a utility. If there is uncertainty over the time there is to recover transaction and transition costs, the consolidating utility will be reluctant to offer a higher price to purchase. This will reduce consolidations.

- Result in LDCs delaying divestiture until their deferral period elapses to minimize risk associated with regulatory uncertainty. This in turn will stifle the progress of commercial negotiations and/or limit the success of their implementation and the continued efforts towards LDC consolidation.

Hydro One submits that the same transactional certainty is appropriate regardless of whether the underlying transaction involves a utility that is already in a deferred rebasing period or not. Given this, Hydro One requests that the OEB clearly articulate in the consolidation Handbook that if an entity is already in the midst of a deferred rebasing period that is the result of a previous acquisition and that entity then gets acquired in a subsequent commercial transaction, the new acquiror should be eligible to receive a full ten-year deferred rebasing period (if requested) from then on to recover the costs associated with the subsequent commercial transaction. The full ten-year deferred rebasing period should be made available to the acquiror without any justification required akin to what would be available to an acquiror of a utility not in a deferred rebasing period as documented in the OEB Handbook. To address OEB Staff's concerns with respect to deferral or rebasing indefinitely', applicants should propose how they would mitigate this risk in their application.

Hydro One encourages the OEB to consider addressing multiple transactions in an Appendix of the OEB MAAD Handbook (or in a separate document altogether), so that it can be updated as new/different scenarios are encountered. Proceeding in this manner, would allow OEB staff to do more targeted consultations going forward without opening the entire Handbook thus improving regulatory efficiency, as needed.

5.0 PERFORMANCE METRICS & REPORTING

The following addresses Hydro One's comments on the reporting recommendations in the Discussion Paper.

6.0 COST EFFECTIVENESS & ECONOMIC EFFICIENCY REPORTING

OEB Staff propose that monitoring of post-consolidation activities may provide benefits to the industry.[17]

It is important to keep in mind that the intent of consolidation is to reduce costs on the distribution system – including regulation. Consequently, Hydro One suggests that the potential benefits of post-consolidation monitoring may be outweighed by the costs of their implementation. For instance:

- Reporting requirements to tell a consolidation "story" are not necessary. They create a regulatory burden that should be avoided. There are avenues other than through reporting requirements to tell the "story" that are likely less burdensome and more effective.

- A consolidating entity should not be required to provide information to other parties considering consolidation on how they can achieve savings. Information on how consolidation savings are achieved is considered proprietary information and should not be made readily available to other competitors. Disclosing that

[17] Staff Discussion Paper – p.29

information could dissipate competitive advantages of the disclosing distributor for any future consolidations.

- Other OEB approvals have reduced requirements for post-project reporting with the OEB being rightfully interested in exception-based reporting. Hydro One highlights that the OEB has reduced the regulatory reporting burden specific to leave to construct (LTC) approvals by removing both the post-construction financial and monitoring log from the list of standard conditions of approval in an LTC application.[18]

OEB Staff have proposed that new consolidation applications that elect to defer rebasing more than five years should file a mid-term report with various suggested minimum requirements to be detailed.[19]

<u>Hydro One submits that any reports should be limited to information that the OEB does not already have and should not be required for items for which the utility is not seeking cost recovery.</u> For example, as part of the conditions of approval, the applicant should inform the Board when integration is completed. If integration has been completed, there should be no further requirements to include in a mid-term report. If a utility is not seeking to recover transaction and/or transition costs in revenue requirement, details specific to progress on whether those costs have been recovered are unnecessary for regulator review.

Hydro One suggest that the OEB establish standard conditions of approval, akin to LTC approvals, such that applicants know in advance what will be expected of them, thus building in any mandatory costs of those requirements into the evidence and appropriately reflecting the savings sans mid-term or other type of reporting expected to come out of the Board's updated consolidation policy. Hydro One acknowledges that in the event of a special circumstance, the OEB would not be confined to these conditions of approval and

[18] The OEB has also made a concerted effort to minimize the regulatory burden on small sized LDCs and continue to make modifications to filing requirements for small sized LDCs in Ontario to alleviate the pressures associated with these requirements.
[19] Staff Discussion Paper – p.30

could impose additional conditions as the OEB deems necessary. However, establishing the minimum conditions of approval will establish the bar of what the OEB deems prudent and cost-effective.

Hydro One does agree with OEB Staff, however, that there could be benefits to a mid-term report if a utility is aware that it is failing to meet the forecast MAAD targets and will not reach those cumulative savings targets by the end of the deferred rebasing period term. This, for example, could be a result of the challenges spoken to in the above sections regarding the inherent challenges of making a pre-acquisition assessment of the target's distribution system assets. To address this possibility, Hydro One suggests mandating a simple condition to have an applicant notify the OEB of any material change in the project akin to what is done in leave to construct applications. This should satisfy the concern. Under this premise, if a utility remains on track to achieve the cumulative targets forecast in the MAAD no reporting is necessary. Conversely, if a utility is facing challenges in meeting their MAAD forecasts, they can inform the Board, accordingly in the proposed mid-term report.

If the OEB does implement reporting requirements as a result of this consultation, Hydro One requests that clear documentation also be provided of how the required reports will subsequently be used by the OEB.

6.1 REPORTING ON KEY PERFORMANCE MEASURES: RELIABILITY & QUALITY OF SERVICE

With respect to reporting on key performance measures, OEB Staff have made several recommendations in the Discussion Paper.

OEB Staff propose that the MAADs filing requirements for consolidation applications be updated to include feeder level information, if available, to assess reliability. Specifically, applicants that have voluntarily filed feeder level information historically leading up to the consolidation application, are expected to provide a listing of feeder reliability by rate zone (i.e. for the predecessor utilities) for the most recently completed historical years available, up to five years. OEB Staff adds that following approval of a consolidation application, OEB staff is of the view that if feeder-level reliability information is available, and if at least one of the pre-consolidation utilities has been reporting feeder level reliability information historically for at least one of the legacy rate zones, the OEB should require the consolidated utility to continue reporting this data for any available rate zone, and identify the rate zone for each feeder during the deferred rebasing period.[20]

Conversely, with respect to service quality, OEB staff proposes that the current practice of consolidated distributors reporting service quality metrics on a consolidated basis post-consolidation continue. In supporting this conclusion, OEB Staff outline that in most situations, the potential cost of tracking and reporting on service quality metrics by rate zone post-consolidation outweighs the potential benefits. OEB staff agrees that there would be an inherent level of inefficiency in tracking results separately given that, typically, distributors in a deferred rebasing period due to consolidation are working toward centralizing functions to potentially achieve efficiencies that will be passed on to customers at the time of the consolidated entity's rebasing application.[21]

There should be no distinction between service quality reporting and reliability reporting. Hydro One agrees with the existing language in the OEB's MAAD Handbook that has been established through previous jurisprudence on this matter.[22] Notably, the OEB has a proactive performance monitoring framework that inherently protects electricity customers from harm related to service quality and reliability and has established the mechanisms to intervene if corrective action is warranted.

<u>No additional reporting requirement on reliability is required nor would any imposed reporting requirement be helpful in assessing whether harm has been caused post-transaction approval.</u> Reliability data is a snapshot in time. SAIDI, SAIFI, CAIDI and/or the recently contemplated voluntary feeder level reliability data proposed from the ongoing Reliability and Power Quality Review (RPQR) consultation, is all predicated on historic information that is not necessarily indicative of future results irrespective of utility ownership. In fact, deterioration of these results during the deferred rebasing (especially in the immediate five years following acquisition) is likely due to the age of the asset and

[20] Staff Discussion Paper – p. 33
[21] Staff Discussion Paper – p. 34
[22] EB-2014-0244 - OEB Decision & Order – March 12, 2015

asset replacement plans (i.e., capital expenditure plans) or maintenance schedules (i.e., OM&A expenditures) that were in effect from the predecessor utility, not from the practices on the new consolidated entity.

Redundant reporting is unwarranted and ineffective. As documented in previous jurisprudence, the OEB has stated that:

> On balance, the OEB does not view the possibility of some service metrics not being maintained consistently at the current level as warranting a refusal of an application. The OEB has a proactive service quality oversight framework and can intervene if action is warranted. [23]

Additionally, with respect to feeder level reliability data, it is important to consider that many consolidations encompass the acquisition of embedded utilities, i.e., LDCs served by an upstream host LDC. <u>Though there may be some capability to segment feeder level reliability data when there are two separate and distinct geographic rate zones, this is not feasible for the elimination of embedded utilities.</u> OEB Staff highlight in the Discussion Paper, and Hydro One agrees, that as time passes and utilities work to integrate systems between merged utilities (where possible), feeders may serve different purposes, rate zones or even multiple rates zones.[24] For embedded utilities, this already exists. An embedded feeder supply can serve upstream host distributor customers, run through the territory of an embedded utility serving customers of the embedded utility, and then serve more customers of the host distributor, downstream. Eliminating the artificial electrical border that exists between these types of utilities and maximizing the benefits of consolidation by eliminating unnecessary metering equipment and repurposing assets and minimizing ratepayer costs, accordingly, is the intent of consolidation. Variances in the information pre and post consolidation cannot be explained away qualitatively as that would require unnecessarily refining and redefining pre-existing artificial electrical borders and making a multitude of assumptions strictly for the purposes of adhering to this proposed reporting condition. That is impractical and lacks merit. <u>For these reasons, the integrity of feeder level reliability data cannot be utilized for the purposes of comparison to the status quo for all embedded utility mergers and acquisitions.</u>

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[23] EB-2014-0244 – OEB Decision & Order – March 12, 2015 – pp. 4-5
[24] Staff Discussion Paper – p. 33

Additionally, the merits of feeder-level reliability are still very much subject to the OEB's consultation on RPQR, and that utilities (including Hydro One) have raised many concerns not yet addressed in that forum. Hydro One submits that consideration of feeder-level reporting in the context of MAADs is therefore premature and should be removed and addressed in the context of the RPQR consultation.

7.0 COST RECOVERY TREATMENT FOR TRANSACTION, TRANSITION, INTEGRATION COSTS

Hydro One does not have any material comments on this specific section of the report and commends OEB Staff for seeking to provide clarity on the items discussed therein.

8.0 INCREMENTAL CAPITAL FUNDING AVAILABILITY TO CONSOLIDATED UTILITIES

Hydro One has no comments on the inflation rate that should underpin the ICM but suggests that such an assessment should be more appropriately considered/reviewed in any prospective review of the OEB's Policy Options for the Funding of Capital Investments (i.e., Incremental Capital Module), should the OEB find that such a review is required. Additionally, Hydro One has not identified any concerns with the existing ICM framework specific to MAADs.

9.0 ACCOUNTING MATTERS

On the proposed accounting matters, Hydro One’s comments are limited to stating that further clarity on the materiality threshold for the divestiture of proposed regulatory accounts would be helpful. Specifically, guidance on whether the materiality to assess divestiture should be predicated on the predecessor utility whose policies have changed, or, in the alternative, it should be predicated on the thresholds of the consolidated entity.

10.0 EARNINGS SHARING MECHANISM (ESM)

With respect to the Earnings Sharing Mechanism (ESM), Hydro One is aligned with OEB Staff that an ESM should be established for a deferred rebasing period longer than five years. Hydro One also supports OEB Staff’s view on a default form of ESM, while maintaining flexibility for utilities to propose an alternative ESM that may better reflect a transaction’s unique circumstances as contemplated in the MAADs Handbook.

Continuing to provide utilities and more specifically potential consolidators, flexibility to propose and implement an ESM that balances the needs of shareholders and protects the interests of ratepayers during the extended deferred rebasing period will continue to support consolidation efforts.

11.0 PERFORMANCE STANDARDS

With respect to performance standards, defining such will be extremely helpful to set expectations for both divesting and acquiring shareholders and for acquirors to plan resources effectively for the seamless implementation of an acquisition or merger. The OEB's current performance standards for MAADs applications is defined by hearing types as discussed in the Discussion Paper – 180 days for an oral hearing or 130 days for a written hearing. Regrettably, this performance standard has not been met in many MAAD applications and Hydro One hopes that with the further refinement of these reporting requirements, adherence to the performance standards can be achieved for future MAAD applications.

Hydro One acknowledges that this missed target is not due to lack of effort and is more so a reflection that no two transactions are identical. Typically, there are many unique scenarios required for a panel to satisfy itself that there will be no harm to customers, and it is imperative that they are diligent in these decisions as transactions cannot be unwound post-approval. Additionally, the continued evolution of the no harm test and the opportunity to defer rebasing beyond a 5-year planning period i.e., the period over which the OEB's rate setting/rebasing regulatory framework is anchored, also has introduced challenges that are unique to MAAD applications. Hydro One does not believe these items were included in the original established performance standards for MAADs.

Hydro One believes that it will be effective for the OEB to review previous MAAD application approval timelines from complete application receipt to the issuance of the final decision. In so doing, the OEB will have a lens on whether the existing timelines reflect actual results and update the performance standards accordingly for what the OEB deems reasonable.

Hydro One recommends that in establishing performance standards the OEB consider whether certain criteria could enable two differing performance standards for MAADs that is more in-line with how the OEB has established differing performance standards for other application types. For both rate and leave to construct applications, the OEB has timelines for complex and non-complex applications based on a multitude of factors. The OEB could establish similar criteria for MAAD reviews with one potential option being the value of the purchase, the size of the utility and/or the potential effect of the transaction on the financial viability of the company acquiring the utility. Hydro One is amenable to have these specific criteria open for further consideration and review.

12.0 OTHER

Hydro One's final comments on the Discussion Paper are with respect to the language regarding proforma financial statements and their requirement in general. Hydro One believes that the OEB should consider minimizing regulatory burden where there's merit in doing so.

For Canadian securities law regulators and securities law purposes, acquisitions that meet certain prescribed significance tests in National Instrument 51-102 are considered "significant" acquisitions, requiring a reporting issuer to file a business acquisition report (or 'BAR') that discloses specific information on the significant acquisition. The BAR requirements include the preparation of, among other items, pro forma financial statements that give effect to the significant acquisition.

Hydro One was questioned by the OEB why they did not file proforma financial statements for the proposed acquisition of CPUC. Notably, that acquisition (and similarly the other previous acquisitions) never triggered the significance tests required under Canadian securities laws for reporting issuers. Hydro One has never had to prepare pro forma financials for security law purposes on the basis that the acquisition was not large enough to hit the trigger level that the Canadian securities regulators have set for significance thus it is unclear what the benefit is to the OEB in this regard. The information sought would require time and cost involved to prepare the financial statements that otherwise have no requirement.

13.0 CONCLUSION

Hydro One thanks the OEB for an opportunity to comment on this Discussion Paper. In refining the no harm test, Hydro One stresses the importance of establishing a reasonable status quo. In-so-doing, the OEB should consider whether an LDC's current system condition in conjunction with their cost structures is commensurate with the future long-term expectations of its customers, the OEB, other regulatory bodies including those overseeing safety, and the anticipated levels of investment required to maintain pace with the increased electrification needs of the distribution system.

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