

## **RÉPONSE À LA DEMANDE DE RENSEIGNEMENTS N° 1 D'HQT-HQD**

### **ÉTABLISSEMENT D'UN MÉCANISME DE RÉGLEMENTATION INCITATIVE ASSURANT LA RÉALISATION DE GAINS D'EFFICIENCE PAR LE DISTRIBUTEUR D'ÉLECTRICITÉ ET LE TRANSPORTEUR D'ÉLECTRICITÉ**

#### **R-3897-2014 – PHASE 1**

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**1. Référence :** Pièce C-OC-0012, p. 8;

**Préambule :**

*« One possibility proposed by PEG could be the use of separate earning sharing mechanisms (ESM), if accepted by the Régie, to distinguish costs and revenues of both classes of customers. »*

**Demandes :**

a. Please provide examples of where ESMs have been established on a class specific basis.

**Réponse :**

**The premise is that as proposed by PEG, there could be different ARMs (“baskets”) for small volume and industrial customers. The corollary is that the realized (actual) return from the two baskets could differ and the appropriate ESM should reflect this.**

b. What advantages does Mr. Belanger perceive associated with class specific ESMs ?

**Réponse :**

**See answer 1 a). One advantage would be lowered risk for small load customers.**

c. What disadvantages does Mr. Belanger perceive associated with class specific ESMs ?

**Réponse :**

**See answer 1 a). One disadvantage would be additional complexity.**

**2. Référence : Pièce C-OC-0012, p. 10;**

**Préambule :**

*“More importantly, OC submits that the continuous efficiency improvements embedded in section 48.1 are best achieved under a MRP with an ARM than under a cost of service MRP. A recent decision by the Ontario Energy Board (OEB) is interesting in that regard. Hydro One Networks Inc. (Hydro One) filed its 2015-2019 Distribution rate application suggesting the use of a multiyear cost of service under the custom incentive rate-setting option. The OEB rejected Hydro One’s Distribution proposal for the five following reasons: [...]”*

**Demandes :**

- a. Please confirm that a multi-year forecast approach is a form of an ARM.

**Réponse :**

**Confirmed. OC agrees with PEG’s definition that an ARM “*automatically adjusts rates to reflect changing business conditions without linking the relief to the utility’s own cost growth*”<sup>1</sup>.**

- b. Please confirm that the referenced decision from the OEB pertains only to Hydro One’s distribution system, and Hydro One files separately for transmission rates.

**Réponse :**

**Confirmed.**

- c. Please confirm that the net outcome of the referenced decision was a multi-year cost of service approach to setting Hydro One’s distribution rates for 2015, 2016, and 2017.

**Réponse :**

**OC confirms the OEB set distribution rates for 2015, 2016 and 2017 for Hydro One using a multiyear COS approach. It did so while at the same time rejecting Hydro One’s Custom Cost of Service request under the RRFE policy, as indicated in the following excerpt<sup>2</sup>:**

*The company indicated that cost savings from productivity improvements were embedded in cost forecasts, and that the company would bear the risk of failing to achieve these savings. The OEB does not consider Hydro One’s “Custom Cost of Service” application to be sufficiently aligned with the objectives of the RRFE policy to approve the*

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<sup>1</sup> C-AQCIE-CIFQ-0025, p. 7.

<sup>2</sup> C-OC-0015, p. 8.

*application as presented. Also, the OEB does not consider it acceptable to postpone the potential commencement of an appropriately-structured incentive based rate setting framework until 2020 following the five year period proposed by Hydro One.*

*The OEB accordingly denies Hydro One's request for five year rate setting. However, the OEB will approve rates for 2015, 2016, and 2017 using a cost of service methodology, based on the evidence filed and tested in the hearing. This results in an increase in distribution revenues of about 19% from 2014 to 2017, compared to Hydro One's request of a 29% increase over a five year period as cited above.*

- d. Please confirm that Hydro One's transmission system continues to be regulated under cost of service regulation.

**Réponse :**

**Confirmed.**

- e. Please confirm that the OEB did approve a multi-year forecast approach for Enbridge for rates in effect for 2015-2018 in EB-2012-0459, July 17, 2014.

**Réponse :**

**Confirmed. Enbridge filed under the Custom IR option with a five-year term forecast of main operating and capital revenue requirement components.**

- f. Please confirm that the OEB did approve a custom IR plan for Toronto Hydro with a multi-year forecast of capital and indexed approach to O&M in EB-2014-0116, December 29, 2015.

**Réponse :**

**Confirmed. Toronto Hydro filed under the Custom IR option with a custom price cap index.**

**3. Référence : Pièce C-OC-0012, p. 12;**

**Préambule :**

*"Concentric does not support benchmarking. It recommends "the Régie rely upon its judgment, with input from the parties, on setting the appropriate productivity factor for HQD"*

**Demande :**

- a. Please confirm that Concentric recommended that the Régie rely on its judgment, but left it to the parties to determine if benchmarking or other statistical studies should inform the Régie's judgment.

**Réponse :**

**In its report, PEG suggests to the Régie that both productivity and extensive benchmarking studies should be commissioned during Phase 2 to inform on the ARM inputs for both divisions. It is OC's understanding that Concentric is not suggesting or supporting such studies for Phase 2.**

**Concentric has expressed views/considerations on many input/output factors. Accordingly, OC does not understand why Concentric leaves it to the parties to determine if benchmarking should be used to inform the Régie on ARM design, including productivity, rather than suggesting from its own experience whether benchmarking is/is not of assistance.**

**We note, as showed in the table below, that in the OEB RRFE Framework Benchmarking is required for Custom IRM Applications<sup>3</sup>.**

**Table 1: Rate-Setting Overview – Elements of the Three Methods**

		4 <sup>th</sup> Generation IR	Custom IR	Annual IR Index
<b>Setting of Rates</b>				
<b>"Going in" Rates</b>		Determined in single forward test-year cost of service review	Determined in multi-year application review	No cost of service review, existing rates adjusted by the Annual Adjustment Mechanism
<b>Form</b>		Price Cap Index	Custom Index	Price Cap Index
<b>Coverage</b>		Comprehensive (i.e., Capital and OM&A)		
<b>Annual Adjustment Mechanism</b>	<b>Inflation</b>	Composite Index	Distributor-specific rate trend for the plan term to be determined by the Board, informed by: (1) the distributor's forecasts (revenue and costs, inflation, productivity); (2) the Board's inflation and productivity analyses; and (3) benchmarking to assess the reasonableness of the distributor's forecasts	Composite Index
	<b>Productivity</b>	Peer Group X-factors comprised of: (1) Industry TFP growth potential; and (2) a stretch factor		Based on 4 <sup>th</sup> Generation IR X-factors
<b>Role of Benchmarking</b>		To assess reasonableness of distributor cost forecasts and to assign stretch factor		n/a
<b>Sharing of Benefits</b>		Productivity factor		
		Stretch factor	Case-by-case	Highest 4 <sup>th</sup> Generation IR stretch factor
<b>Term</b>		5 years (rebasings plus 4 years).	Minimum term of 5 years.	No fixed term.
<b>Incremental Capital Module</b>		On application	N/A	N/A
<b>Treatment of Unforeseen Events</b>		The Board's policies in relation to the treatment of unforeseen events, as set out in its <a href="#">July 14, 2008 EB-2007-0673 Report of the Board on 3<sup>rd</sup> Generation Incentive Regulation for Ontario's Electricity Distributors</a> , will continue under all three menu options.		
<b>Deferral and Variance</b>		Status quo	Status quo, plus as needed to track capital spending against plan	Disposition limited to Group 1 Separate application for Group 2
<b>Performance Reporting and Monitoring</b>		A regulatory review may be initiated if a distributor's annual reports show performance outside of the $\pm 300$ basis points earnings dead band or if performance erodes to unacceptable levels.		

**4. Référence : Pièce C-OC-0012, p. 14;**

**Préambule :**

*“Following the introduction of a revenue cap ARM for HQT, OC recommends having Y and Z factors for HQT. The stairstep pattern of HQT capex indicates that providing an optional treatment for some capital projects is appropriate. OC notes that the ICM implemented by the OEB provides clear guidelines to the Y-factoring of CapEx. Under the ICM, incremental capital can be included if it meets the eligibility criteria as reproduced below: [...]”*

**Demandes :**

- a. Please confirm that the cited filing requirements by the OEB from June 2011 pertain to the prior generation of incentive regulation for electric distributors, which has been replaced by the Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach (RRFE), adopted October 18, 2012.

**Réponse :**

**OC confirms that the base filing requirements document is as cited. However, the OEB has issued annual updates to reflect the RRFE. The latest update is for 2016 rates (issued in July 2015).**

- b. Is OC aware of any prior concerns expressed by utilities regarding the allowance of capital projects under the OEB's Incremental Capital Module?

**Réponse :**

**No. OC did not research utility concerns.**

- c. In which of the OEB's options under its latest incentive regulation framework for electric distributors is the Incremental Capital Module allowed, and how many utilities have applied under this option?

**Réponse :**

**The OEB RRFE Filing Guidelines<sup>4</sup> indicate an ICM may be requested under the 4GIRM. Distributors may also request an allowance for capital in some form under Custom IRM (such as the Toronto Hydro Application).**

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[http://www.ontarioenergyboard.ca/oeb/\\_Documents/2016EDR/OEB\\_Filing%20Requirements\\_2016Rates\\_Chapter%203.pdf](http://www.ontarioenergyboard.ca/oeb/_Documents/2016EDR/OEB_Filing%20Requirements_2016Rates_Chapter%203.pdf)

As of January 15 2016, we understand that Ontario electricity distributors (other than Toronto Hydro) have applied for either 4GIRM with an ICM or Custom IR plans :

- **4GIRM with ICM : Enersource**
- **Custom IRMs : Horizon, Kingston, Hydro Ottawa, Oshawa Hydro, Powerstream.**

**5. Référence : Pièce C-OC-0012, p. 17;**

**Préambule :**

*“OC recommends the adoption of PEG’s performance metric system. OC suggests two proposals for PIMs for HQD need special consideration. They are not included in the Concentric Report. The first is the peak load savings indicator. The motivation for its incentivization is straightforward as it aims to provide “incentive to reduce peak loads”. Peak load savings might be difficult to estimate and need meticulous computations, but overall OC thinks it would provide the needed incentives for HQD to address current peak load problem. Incentivization of CDMs was applied to Gaz Métro’s MRP. The other indicator suggested by PEG that needs special consideration is the power supply cost PIM. Although it is difficult to see how it would work in practice as of now, OC thinks the proposition should be explored as of phase 3.” (References omitted)”*

**Demandes :**

5.1 Does OC believe that performance metrics, to be effective, should reasonably be within management’s control?

**Réponse :**

**In general yes but deviations and/or exceptions should be reported as well.**

5.2 Is OC aware of any North American electric distribution utility that has an incentivized power supply cost provision?

**Réponse :**

**No. The issue is the intercorporate relationship between the Producer and the Distributor. Accordingly there is no incentive for the Distributor to reduce its power costs, including its peak demand.**