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BY EMAIL

March 6, 2014

Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
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2300 Yonge Street
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BoardSec@ontarioenergyboard.ca

Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Enbridge Gas Distribution Inc. ("Enbridge")
Board Staff Submission
Board File No. EB-2014-0043

In accordance with Procedural Order No. 1, please find attached the Board staff submission relating to the above proceeding.

Enbridge's Reply Submission, if it intends to file one, is due by March 11, 2014.

Yours truly,

Original Signed By

Daniel Kim
Case Manager

cc: All parties EB-2012-0459

ONTARIO ENERGY BOARD

BOARD STAFF SUBMISSION

Enbridge Gas Distribution Inc.

EB-2014-0043

March 6, 2014

Board Staff Submission
Enbridge Gas Distribution Inc.
EB-2014-0043

Introduction

Enbridge Gas Distribution Inc. ("Enbridge") filed an application with the Ontario Energy Board (the "Board") on February 13, 2014 under section 36 of the *Ontario Energy Board Act*, *1998*, S.O. 1998, c. 15, (Schedule B) for an order giving final approval for Rider C commodity unit rates that were approved on an interim basis in the Board's EB-2013-0406 Decision and Interim Order, dated December 20, 2013. Enbridge indicated that the $10.1 million should have been refunded to sales (i.e. system gas) service customers in prior Quarter Rate Adjustment Mechanism ("QRAM") applications but were not, due to calculation errors. Rider C commodity unit rates were approved on an interim basis because the proposed refund of $10.1 million raised possible concerns of rate retroactivity.

The Board in its Procedural Order No. 1, dated February 27, 2014, noted that parties in the EB-2013-0406 proceeding had an opportunity to file responsive comments, therefore, the Board considered the record in this proceeding to be sufficiently clear. The Board also in its Procedural Order No. 1, invited parties and Board staff to make submissions on the issue of rate retroactivity.

Issue

Does the proposed refund of $10.1 million raise issues of rate retroactivity?

Board Staff Position

Board staff submits that the Board should approve, on a final basis, the Rider C commodity rates approved on an interim basis in EB-2013-0406.

Background

Enbridge's EB-2013-0406 application was filed in accordance with the QRAM process for a rate adjustment relating to gas costs effective January 1, 2014 ("QRAM Application"). In that application, among other things, Enbridge proposed a refund of $10.1 million from the Gas Acquisition – Commodity and the Gas in Inventory Re-valuation components of the Purchased Gas Variance Account ("PGVA"). The

proposed refund is a result of calculation errors made by Enbridge with respect to balances in the PGVA. Enbridge indicated that the $10.1 million should have been refunded to sales (i.e. system gas) service customers in two prior QRAMs (October 2012 and April 2013).

Nature of the Errors

Enbridge identified two errors discovered from previous QRAM proceedings. Specifically, Enbridge indicated that it has discovered a "mechanical error" from the October 2012 QRAM that resulted in ratepayers not being credited with $7.8 million to which they were entitled and a further mechanical error from the April 2013 QRAM which resulted in ratepayers not being credited with $2.3 million to which they were entitled[1]. Enbridge proposed to refund this $10.1 million to ratepayers in the January 1, 2014 QRAM Application.

The mechanical errors came to light during an internal review made by Enbridge with respect to previous QRAM calculations. This review revealed that two formulae within Excel spreadsheet models were incorrectly summing the line items for the determination of the Gas Acquisition – Commodity Component of its PGVA balance for its October 2012 QRAM, as well as, the determination of its Gas in Inventory Re-valuation PGVA balance for its April 1, 2013 QRAM.

Nature of the QRAM

The QRAM process approved by the Board for Enbridge comprises the following components: the calculation of a forecast price for rate-making purposes during a test year (“utility price”); the means of adjusting the utility price for rate-making purposes during a test year; the means of calculating and clearing variances in Enbridge’s PGVA; the regulatory framework for approving adjustments and clearances; and the means of providing pricing information to end-use customers, or their marketers, and to other stakeholders as well[2].

In response to Board staff Interrogatory #1c in the QRAM Application proceeding, Enbridge stated that the proposed corrections did not raise a retroactivity issue because the rider (i.e. Rider C), inclusive of corrections, would be applied to customers’ bills on a prospective basis. Enbridge also noted that in accordance with the Board-approved

[1] Exhibit B, Tab 2, Schedule 1, pp. 3-6.
[2] EB-2013-0406, Enbridge’s QRAM Application, Exhibit Q1-1, Tab 2, Schedule 1, Appendix A, p. 1

methodology, the derivation of Rider C unit rates within a QRAM application reflect both forecast and actual balances for the components of the PGVA, as well as a true-up mechanism of over and under collections or refunds to customers. Therefore, Enbridge is of the view that the two proposed corrections from previous QRAMs could be viewed in the same manner as the true-up mechanism, which currently exists within the QRAM methodology.

Submission

Rule against Retroactive Ratemaking

It is a well-known principle that economic regulatory tribunals must exercise their rate making authority on a prospective basis, unless the governing statute specifically contemplates otherwise. Generally speaking a tribunal cannot exercise its authority retroactively by making "out of period" determinations. There are several justifications for this principle: first, both distributors and consumers are entitled to certainty respecting the rates for which they are responsible, and should generally not be made to "top-up" or adjust down those rates after they have already been paid[3]. Second, charging consumers through current rates for out of period costs will likely result in inter-generational inequity, whereby the consumers that were responsible for the costs may not be the same consumers paying the costs[4]. Third, it prevents tribunals from improperly disgorging distributors of any legitimate over-earnings after the fact[5].

As such, when an issue is raised through an application which suggests that a party is requesting to adjust amounts already considered through previous final rate orders, there is a concern about rate retroactivity since a final rate order may not be varied. In this application, Enbridge is requesting that the Board allow the two proposed corrections from previous QRAMs on the basis that the corrections themselves are in the nature of a true-up mechanism for commodity pass-through accounts, which currently exists within the QRAM methodology.

There are a number of exceptions to the rule against retroactivity. For example, deferral and variance accounts do not violate the rule against retroactivity because they are identified by the Board on a prospective basis. Although the exact amounts ultimately held in the deferral accounts are not known prospectively, the Board identifies up-front

[3] *Calgary (City) v. Alberta (Energy and Utilities Board), 2010 ABCA 132.*
[4] *R. v. Board of Public Utilities Commissioners (1966), 60 D.L.R. (2d) 703 (N.B.S.C.A.D.).*
[5] *Bell Canada v. Canada (CRTC), [1989e] 1 S.C.R. 1722.*

that the revenues/costs that enter these accounts are “encumbered”, and subject to future disposition. Deferral accounts are regarded as "accepted regulatory tools" to be operated as part of rate-setting powers[6].

The PGVA in issue in this application is an ongoing variance account which tracks the difference between the utility payments to the market suppliers and payments recovered from customers for the energy commodity. These variances are included in the establishment of the rate rider unit rates for the next 12-month period. The question which is addressed below is whether allowing a change to the final rates established by the two previous QRAM decisions amounts to retroactive ratemaking.

Review of Relevant Case Law

In considering the issue of rate retroactivity, specifically with respect to accounts in the nature of the PGVA, Board staff reviewed the treatment of these types of accounts in other jurisdictions to determine if the issue of rate retroactivity has been addressed. In a decision of the Alberta Energy Utilities Board (“AEUB”) (EUB Decision 2006-042)[7], the AEUB made determinations with respect to out of period adjustments to a Deferred Gas Account (“DGA”) and further, the AEUB examined the merits of establishing a limitation period for adjustments to a DGA. Ultimately the AEUB allowed for the adjustment and the City of Calgary appealed to the Alberta Court of Appeal. The discussion set out in the Alberta Court of Appeal decision is helpful in considering how the Court approached the issue of rate retroactivity. Further, the Court commented on the principles of certainty and finality in a final rate order and intergenerational inequity and whether or not it should hear a case where there is a request for a retroactive adjustment to a final rate order.

By way of background the facts are such that in May 2004, ATCO sought approval from the AEUB to correct balances in the DGAs for each of its south and north gas distribution service territories. The proposed adjustment to the DGA for northern Alberta was largely attributable to overstated gas costs from January 1998 to February 2004, whereas in southern Alberta the actual gas costs ATCO incurred from January 1999 to February 2004 were understated. ATCO proposed that its present southern Alberta

[6] *Dow Chemical Canada Inc. et al and Union Gas Ltd* (1983) 42 O.R. (2d) 731
[7] EUB Decision 2006-042: *ATCO Gas -- A Division of ATCO Gas and Pipelines Ltd., (This Decision is also applicable to Direct Energy Regulated Services and AltaGas Utilities Inc.), Deferred Gas Account Limitation Period*, Application No. 1407502, May 11, 2006. The determinations in this decision were subsequently supported in AUC Decision 2010-437, ATCO Gas Measurement Adjustments Outside of the Deferred Gas Account Limitation Period, Application No. 1606079, Proceeding ID. 587, September 9, 2010.

consumers would pay the shortfalls and that it would refund excesses to its present northern Alberta consumers.

The City of Calgary argued that the Board's jurisdiction was limited by section 40 of the Gas Utilities Act (see para. 27) such that "the Board's jurisdiction to consider prior period financial activity of a utility is limited to a 12-month period, even when the financial activity occurs in a deferral account approved by the Board": p. 7. The Board disagreed, partly because of its interpretation of its broad statutory mandate to fix just and reasonable rates.

The Board allowed for 85% of the requested adjustments and the City of Calgary appealed.

As noted above, the AEUB decision was appealed to the Alberta Court of Appeal (the "Deferred Gas Account Decision").

One of the issues considered by the Court of Appeal was framed as follows:

> "Issue 2. Did the Board retroactively change rates or did its decision have a prohibited effect?"

At para. 50 the Court stated:

> [50] In this case, the proposed accounting adjustments had retrospective effect: past costs would be borne by ATCO's present southern Alberta consumers, not the 1999 - 2004 consumers who received gas utility services when ATCO's gas costs were incurred.
>
> [51] In summary, whether termed retrospective or retroactive ratemaking, imposing gas cost shortfalls or surpluses incurred by past consumers on future consumers is generally prohibited. Although this prohibition against retroactive and retrospective ratemaking is relatively clear, how to apply it in practice is less so. A review of key cases illustrates the complexity.

The Court then went on to review the relevant case law with respect to the rule against retroactive ratemaking and noted the following:

> [57] Both Bell Canada 1989 and Bell Aliant (which concerned deferral accounts rather than interim rates) illustrate the same preoccupation: were the affected parties aware that the rates were subject to change? If so, the concerns about predictability and unfairness that underlie the prohibitions against retroactive and retrospective ratemaking become less significant.
>
> [58] Were these parties aware that gas rates were potentially subject to change through the use of the DGA? If so, whether the rates are characterized as interim or final, the principles in Bell Aliant govern.
>
> [59] The history of DGAs demonstrates that affected parties knew they would be used from time to time to alter gas rates based on later, actual gas costs. Reconciliation of the DGA/GCRR would sometimes benefit consumers and sometimes not. Gas rates sometimes changed because of the lack of predictability (volatility) in gas prices and sometimes from other factors such as measuring errors. Whatever the cause, the objective was to ensure that the consumer paid the actual cost of the gas. This legitimate object was accepted by all parties. It strengthened the utility regulatory system by ensuring that the utility received a fair rate of return on its rate base.

Ultimately the Alberta Court of Appeal found that the use of the DGA in this case did not involve prohibited ratemaking given the nature and purpose of the account however, the Court of Appeal did find that the decision of the AEUB in permitting the retroactive adjustment was not reasonable.

In reaching this decision the Court noted several findings that were made by the AEUB the first of which was when first implemented, reconciliations of the DGA were not expected to go back further than 12 months. Longer periods were sometimes accepted under special circumstances. Further, the DGA “was never set up with the intention of permitting all prior period accounting errors, particularly those that would have been subject to ATCO’s management and control”. Other factors noted by the Court include: accounting errors should typically be absorbed by the utility’s shareholders; the DGA should not be treated as a catch-all for fixing errors, including those with a long history or resulting from human error, when adequate processes have not been in place to capture and correct the problem at an early stage; seven years represents a significant lag presenting obvious inter-generational equity issues; ATCO had an onus to ensure its system was working properly and was providing correct data; it did not appear that

ATCO implemented an appropriate and timely review process for its system design; and there was a lengthy delay in discovering the errors. With respect to the delays the Court stated that the long delays gave rise to inter-generational equity issues which lie at the heart of the prohibition against retrospective ratemaking.

The Deferred Gas Account Decision was referred to by the Alberta Court of Appeal in a recent decision issued in January 2014. While the subject matter of the case is distinguishable the Court of Appeal did make comment on retroactive ratemaking at para. 56 and 57 of the decision, the Court stated, in referencing the Deferred Gas Account Decision:

> Simply because a ratemaking decision has an impact on a past rate does not mean it is an impermissible retroactive decision. The critical factor for determining whether the regulator is engaging in retroactive ratemaking is the parties' knowledge. Hunt JA stated at para. 57:
>
> - Both Bell Canada 1989 [Bell Canada v. Canada (Canadian Radio-Television and Telecommunications Commission), [1989] 1 SCR 1722] and Bell Aliant [Bell Canada v. Bell Aliant Regional Communications, 2009 SCC 40, [2009] 2 SCR 764] (which concerned deferral accounts rather than interim rates) illustrate the same preoccupation: were the affected parties aware that the rates were subject to change? If so, the concerns about predictability and unfairness that underlie the prohibitions against retroactive and retrospective ratemaking become less significant. (Emphasis added.)[8]

It is clear from the above reference to the Supreme Court of Canada's decision in Bell Canada that an important factor for the Board to consider in determining if the prohibition against retroactivity is engaged, is whether the affected parties were aware that the rates were subject to change. Board staff submits that the nature of the PGVA is that it is subject to change albeit it is explicitly limited to capturing variances over a 12-month period.

[8] Atco Gas and Pipelines Ltd v. Alberta (Utilities Commission) 2014 (ABCA) 28

Submission

Board staff submits that in the current circumstances it would be appropriate to allow the $10.1 million to be returned to ratepayers. Board staff is mindful of the prohibition against retroactive ratemaking, and concedes that much of the relevant case law suggests that the October 2012 and April 2013 QRAM orders were final and therefore not subject to further adjustment. Board staff must also disagree with Enbridge's position that the proposed refund is not retroactive because it is being applied on a prospective basis. All changes to previous orders are done prospectively (indeed absent the ability to travel backwards in time they have to be); the question is whether the order seeks to make an out of period adjustment for a rate that had previously been declared final.

Despite this, Board staff supports Enbridge's proposal to return the money to ratepayers. The underlying rationale behind the rule against retroactivity is: rate certainty (i.e. once a rate is declared final, parties should have confidence that the rate will not later be changed), inter-generational inequity, and preventing a tribunal from disgorging a utility from legitimate over-earnings. Board staff submits that none of these three concerns are actually at issue in the current case.

Regarding rate certainty, it appears to be the position of all parties that this money should be refunded to ratepayers. To the extent there is any entitlement to rate certainty, it has effectively been waived by the parties. No party will be negatively impacted by the proposed refund. Ratepayers will receive money that should have been theirs all along. Enbridge is not actually "out" any income – it is simply returning money that did not properly belong to it in the first place.

Given the relatively short time frame, there is also little concern regarding inter-generational inequity. Even the first error (i.e. the failure to include $7.8 million in the October 2012 QRAM) was less than 18 months ago. There are any number of deferral or variance accounts that are not disposed of for periods longer than 18 months. The customer base is largely the same now as it was in October 2012. In any event, Enbridge's proposal is a straight refund to customers. The public interest in returning money to customers that is properly theirs outweighs any very minor issues of inter-generational inequity.

Finally, there is no issue here with respect to improperly disgorging a utility of its profits. The $10.1 million should always have belonged to ratepayers; it was only because of an accounting error that it was not returned earlier. Further, it is Enbridge itself that proposes to return the money.

It should further be observed that the accounting errors that resulted in the wrong amount being recovered from or refunded to ratepayers in October 2012 and April 2013 were made by Enbridge. Board staff accepts that the errors were completely inadvertent. Regardless, it is a utility's responsibility to keep accurate accounting records, and a utility should not be permitted to benefit financially at the expense of ratepayers for its own accounting errors. As an American decision held: "A utility that misleads or fails to disclose information pertinent to whether a rate-making proceeding should be initiated or to the proper resolution of such a proceeding cannot invoke the rule against retroactive rate making to avoid refunding rates improperly collected."[9] Although Board staff does not suggest that Enbridge in any way deliberately misled the Board or withheld information, the principle that a utility should not benefit as a result of its own errors is a good one.

To allow such a result could even create a perverse incentive for utilities to be less than rigorous in calculating their QRAM balances (though Board staff again stresses that there is no suggestion that this was a motivating factor for Enbridge in the current case). It could also reduce public confidence in the fairness of the Board's orders.

Put simply, to deny Enbridge's request to return the $10.1 million to ratepayers would be an inequitable, even unreasonable, result. The Board is charged with making rate orders that are both just and reasonable. There is no question that the $10.1 million properly belongs to ratepayers, and all parties agree it should be refunded. Although the rule against retroactive ratemaking is generally grounded in sound principles, none of those principles actually apply in the current circumstances. Slavish adherence to a rule that produces (under the current circumstances) an unreasonable result will not produce a just and reasonable rate.

All of which is respectfully submitted

[9] *MCI Telecommunications v. Public Service Commission*, 840 P.2d 765 (Utah 1992)