

**Ontario Energy
Board**
P.O. Box 2319
27th Floor
2300 Yonge Street
Toronto ON M4P 1E4
Telephone: 416- 481-1967
Facsimile: 416- 440-7656
Toll free: 1-888-632-6273

**Commission de l'énergie
de l'Ontario**
C.P. 2319
27e étage
2300, rue Yonge
Toronto ON M4P 1E4
Téléphone; 416- 481-1967
Télécopieur: 416- 440-7656
Numéro sans frais: 1-888-632-6273



BY EMAIL

March 2, 2010

Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge St., 27th Floor
Toronto ON M4P 1E4

Dear Ms. Walli:

**Re: Enbridge Gas Distribution Inc.
2010 Rates
Board File No. EB-2009-0172
Staff ROE Submission**

Dear Ms. Walli:

Please find attached the Board Staff Submission for the above proceeding. Please immediately forward the attached document to Enbridge and all intervenors in this proceeding.

Yours truly,

Original signed by

Colin Schuch
Case Manager

Encl.

IN THE MATTER OF the *Ontario Energy Board Act 1998*,
S.O.1998, c.15, (Schedule B);

AND IN THE MATTER OF an Application by Enbridge Gas Distribution Inc. for an Order or Orders approving or fixing just and reasonable rates and other charges for the sale, distribution, transmission and storage of gas commencing January 1, 2010.

BOARD STAFF SUBMISSIONS

RETURN ON EQUITY FOR USE IN 2010 EARNINGS SHARING

The ROE Issue

On December 11, 2009 the Board issued its 2009 Cost of Capital Report ("2009 Report").¹ The 2009 Report updated the ROE Formula to be used by utilities ("2009 ROE Formula"). Shortly after the issuance of the 2009 Report, Enbridge filed an update to its application, stating that the 2009 ROE Formula should be used for the purposes of calculating the 2010 earnings sharing as set out in section 10.1 of its IRM Settlement Agreement (the "IRM Agreement"). The Industrial Gas Users Association advised the Board it was of the view that the ROE methodology in existence at the time the IRM Agreement was entered into should be used, and requested that the Issues List be amended to add the issue.

The Board's Procedural Order No. 6, issued on February 18, 2010, added Issue 17 to the final Issues List. Issue 17 reads as follows:

17. Does the calculation of the earnings sharing referred to in Section 10.1 of the IRM Settlement Agreement require the use of an ROE based on the Board's cost of capital policy in effect at the time the IRM settlement Agreement was entered into, or the 2009 Cost of Capital Report, which is in effect at the time the earnings sharing calculation will be performed? (the "ROE Issue")

The Procedural Order outlined a process for the filing of written submissions on the ROE Issue by the parties.

¹ See December 11, 2009: *EB-2009-0084 Report of the Board on the Cost of Capital for Ontario's Regulated Utilities*.

Board Staff's Submissions

Board staff submits that the ROE methodology in effect at the time the IRM Agreement was reached ("2008 ROE Formula") should be used for the 2010 earnings sharing calculation. Board staff's reasoning is outlined below.

IRM Settlement Agreement

The IRM Settlement Agreement was entered into on February 4, 2008. It is in place for five years; this is the third year of its term. Board staff submits that the purpose of an IRM is, among other things, to promote consistency, predictability and regulatory efficiency.

Section 10.1 of the IRM Agreement addresses the earnings sharing mechanism. It states:

10.1 Should an ESM be included in the IR plan?

- Complete Settlement: The Parties agree that the IR Plan shall include an earnings sharing mechanism ("ESM") that shall be used to calculate an earning sharing amount, as follows:

- (i) if in any calendar year, Enbridge's actual utility ROE, calculated on a weather normalized basis, is more than 100 basis points over the amount calculated annually by the application of the Board's ROE Formula in any year of the IR Plan, then the resultant amount shall be shared equally (i.e., 50/50) between Enbridge and its ratepayers;

- (ii) for the purpose of the ESM, Enbridge shall calculate its earnings using the regulatory rules prescribed by the Board, from time to time, and shall not make any material changes in accounting practices that have the effect of reducing utility earnings;

- (iii) all revenues that would otherwise be included in revenue in a cost of service application shall be included in revenues in the calculation of the earnings calculation and only those expenses (whether operating or capital) that would be otherwise allowable as deductions from earnings in a cost of service application, shall be included in the earnings calculation.

Enbridge has argued that the language of section 10.1 requires the 2009 ROE Formula to be used for the earnings sharing calculation, and that all other calculations in the IRM Agreement use the 2008 ROE Formula.

Board staff submits that the plain and ordinary meaning of section 10.1 is that the calculation of the earnings sharing is to be done annually, in each of the five years of the IRM Agreement, using the ROE Formula in place at the time the IRM Agreement

was entered into, that is, the 2008 ROE Formula. Board staff submits that to interpret the clause to require the use of the 2009 ROE Formula would introduce an element of unpredictability for one calculation out of the many that must be made over the duration of the IRM Agreement; and that such an interpretation would conflict with the goals of an IRM which is to promote consistency, predictability and regulatory efficiency.

Cost of Capital Report of the Board

Board staff submits that the 2009 Report supports the position that the legacy 2008 ROE Formula is to be applied throughout the duration of the IRM Agreement. In the Executive Summary and in the Annual Update Process (section 6.1) the 2009 Report states:

The Board will apply the methods set out in this report annually to derive the values for the return on equity and the deemed long-term and short-term debt rates for use in cost of service applications. (Emphasis added)²

Board staff also notes that the 2009 Report states in section 5.1:

The policy set out in Chapter 4 of this report will come into effect for the setting of rates, beginning in 2010, by way of a cost of service application. (Emphasis added)³

The words in the 2009 Report contemplate that the Board felt it necessary to implement the new ROE and debt methodologies in a cost of service application, when all aspects of a utility's revenue requirement can be examined.

Clearly the intent of the Board is that a utility's ROE will be reset at such time as a cost of service application is filed. This makes sense, because many financial parameters are tested, judged, and set or reset as the case may be, at the time of a cost of service review. It also makes sense because to introduce an important revision to a key financial parameter – such as ROE – within an IRM plan mid-term in isolation, would necessarily upset the overall financial balance established in the based rates and the IRM rate adjustment plan as originally agreed upon by the parties.

Board staff submits it is clear that the 2009 Report intended that the 2009 ROE Formula and other updated methods would be applied on a going forward basis, but only for use in cost of service applications. Board staff notes that as Enbridge is in the third year of a five year IRM Agreement, the 2009 ROE should not be applied.

All of which is respectfully submitted.
March 2, 2010

² Ibid, Report on Cost of Capital page iii (Executive Summary) and again at page 63.

³ Ibid, Report on Cost of Capital paragraph 5.1, page 61.