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January 25, 2008

**DELIVERED BY COURIER**

Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street
27TH Floor
Toronto, ON M4P 1E4

Dear Ms Walli:

**Re: Enbridge Gas Distribution Inc. : 2007 CASDA Application**
**Board File: EB-2007-0731**

We enclose two copies of the Reply Argument of Enbridge Gas Distribution Inc. ("EGDI"), together with six bound copies, and one unbound copy, of EGDI's Book of Authorities in respect of the above-noted Application.

An electronic copy of EGDI's Reply Argument, in searchable / unrestricted PDF format, is being forwarded to you contemporaneously with this letter.

We would be pleased to provide Intervenors with a hard copy of EGDI's Book of Authorities, upon request.

Yours very truly,

**AIRD & BERLIS LLP**

*Original signed by*

Dennis M. O'Leary
DMO/ct

c.c. Patrick Hoey, Enbridge Gas Distribution Inc.
Intervenors in EB-2007-0731

EB-2007-0731

**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 the balance and clearance of the Class Action Suit Deferral Account;

**AND IN THE MATTER OF** an application by Enbridge Gas Distribution Inc. for an order or orders amending or varying the rates charged to customers for the sale, distribution, transmission and storage of gas commencing January 1, 2008.

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# REPLY ARGUMENT OF ENBRIDGE GAS DISTRIBUTION INC.

## January 25, 2008

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## A. Introduction and Overview

1. Enbridge Gas Distribution ("EGD" or the "Company") is applying to the Ontario Energy Board (the "OEB" or the "Board"), pursuant to section 36 of the *Ontario Energy Board Act*, *1998* as amended (the "OEB Act"), for an Order or Orders approving the current balance in the Class Action Suit Deferral Account (the "CASDA"), and the disposition of that balance.[1] The amounts currently included in the CASDA, as of December 31, 2007, total $23,545,001, along with interest totalling $1,165,002.[2] EGD seeks recovery of the full balance in the CASDA over several years, with interest, with the recovery to be allocated on the basis of customer numbers.[3]

2. The Company filed its Application and two volumes of prefiled evidence on September 28, 2007 and the Board issued Procedural Order No. 1 on November 23, 2007. The Procedural Order provided parties with the opportunity to ask interrogatories of the Company before filing written argument. Only one interrogatory was asked[4], leaving the factual record filed by EGD unchanged and unchallenged.

3. On January 8, 2008, Union Gas Limited ("Union") and the Electricity Distributors Association filed written argument in support of the Company's Application, and Board Staff filed submissions that took no position on the Application, but asked parties to address several questions about the implications of implementing the clearance of the CASDA over a period shorter than the proposed eight years. On January 11 and 14, 2008, other Intervenors filed argument. The Consumers Council of Canada ("CCC"), who represent "the interests of the broad array of the consumers of natural gas in Ontario"[5], including "the interests of residential customers"[6] indicated that it is generally supportive of the relief sought by EGD and set out the reasons why EGD should be entitled to this relief. Industrial Gas Users Association ("IGUA"), School Energy Coalition ("SEC") and Vulnerable Energy Consumers Coalition ("VECC") filed argument opposing recovery.

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[1] As set out in the Application, the Company also requests that the 2007 CASDA be continued in 2008.
[2] There have been modest additional amounts included in CASDA, totalling approximately $8,000, since the date of Application, related to the completion of Mr. Garland's appeals about his level of compensation; in addition, the interest has continued to accrue since the date of Application.
[3] Ex. A-1-2, p.1; given that the recovery will occur over a number of years, EGD is seeking the continued existence of a CASDA for each of those years.
[4] The interrogatory was asked by SEC, and asked about the allocation of LPP revenues to EGD's rate classes in the years from 1981 to 2002.
[5] Intervention application of CCC, November 7, 2007, at p. 1.
[6] *Ibid*.

4. As this is the first opportunity for EGD to make argument in this proceeding, this submission represents both the Company's Argument-in-Chief and Reply to the arguments filed by various Intervenors. Accordingly, before replying to issues raised by Intervenors, this Argument will summarize the factual history and evidence which provides the basis for the OEB to grant the relief sought.

5. At the outset, EGD submits that it is important to note several important matters and factual realities for which there is no dispute between any of the parties to this proceeding. Stated differently, it is submitted that the Board is capable of making the following findings and drawing the following conclusions based upon the evidence and argument before it.

**a) What factually occurred is not in dispute**

6. The Application consists of a comprehensive and detailed summary of all relevant matters relating to the development and implementation of the late payment penalty ("LPP") and the Garland lawsuit. Not one Intervenor or Board Staff asked for any additional factual information or clarification.[7] No party in any way challenges the evidentiary record. Accordingly, there are a number of facts important for the purposes of allowing recovery, which the Company submits are not in issue. These include:

    i) The purpose of the LPP was solely to benefit ratepayers by the discouragement of delinquent and late payers, thereby reducing the administrative and carrying costs associated with such conduct, with the forecast of LPP revenues being applied to reduce the Company's revenue requirement. In short, the record demonstrates that all of the actions undertaken by EGD in respect of the LPP were well intentioned, and in the best interests of ratepayers. There is no suggestion in any argument to the contrary.

    ii) Support for the LPP by Intervenors has been continuous. Not only do Intervenors fail to reference any concern expressed about the LPP at any relevant time, the fact is that in the Company's annual rate cases, Intervenors supported the continuation of the LPP and enjoyed the benefits of LPP revenues throughout the entirety of the prosecution of the Garland lawsuit. Intervenors and the Board were kept apprised of developments throughout. No Intervenor expressed any concern about the legality of the LPP at any relevant time.

    iii) The LPP could not be changed without a Board Order. Not surprisingly, no party has argued that the Company should have unilaterally implemented a different LPP without Board Order. Equally important, no Intervenor group was prepared to allege in argument that they would have supported a change to the LPP prior to 2001. Given the

[7] The sole interrogatory received asked for further detail in respect of historic LPP revenue allocations.

amount by which LPPs reduced EGD's revenue requirement each year, even if EGD proposed a reduction in the LPP in response to the Garland Statement of Claim, there is no evidence or certainty that Intervenors and/or the Board would have approved such a change.

iv) EGD was obligated to defend the lawsuit. No Intervenor takes the position that the Garland lawsuit should not have been vigorously defended. Indeed, it is clear that ratepayer groups expected such a defence. The fact that Intervenors consented to the recovery of defence legal costs and disbursements on a number of prior occasions confirms that such costs were considered a cost of service associated with carrying on a natural gas distribution business. No Intervenor directly challenges the Company's request for the recovery of legal fees and disbursements associated with its defence.[8]

**b) CCC generally supports recovery**

7. It is important to note that under the proposal to allocate recovery of the CASDA on the basis of customer numbers, the ratepayer group which would have responsibility for the vast majority of the amounts payable is represented by CCC, yet it generally supports recovery by the Company. Stated differently, the ratepayer group which will be responsible for about 90 percent of the CASDA amounts accepts that recovery through rates is generally appropriate.

**c) Intervenors opposed cite no precedents**

8. It is also important to note that no Intervenor opposing recovery referenced any legal or regulatory precedent, text or academic work in support of their position. While several parties refer generally to rate retroactivity and inter-generational issues, to which EGD responds specifically later in this Argument, none cite any precedent or authority to the effect that such issues have led any Court or regulator in any jurisdiction to conclude that recovery in similar circumstances should be denied.

**d) The Board has jurisdiction to order recovery**

9. While several parties quote from the second decision of the Supreme Court of Canada[9], no Intervenor argues that the OEB lacks the legal authority or jurisdiction to approve the recovery in rates of any amount recorded in the CASDA. The Supreme Court of Canada's decision in no way limits the OEB's jurisdiction to consider allowing recovery in rates for the prudent settlement of a civil lawsuit.

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[8] SEC does not address the point at all and VECC requests an audit of defence costs. However, VECC's position goes to quantum, not the right of recovery. EGD responds to VECC's submission on this point later in the Argument.
[9] *Garland* v. *Consumers' Gas Co.*, [2004] 1 S.C.R. 629 (Garland #2 – issued April 2, 2004): Ex. C-1-11.

**e) Garland settlement was prudent**

10. Finally, and perhaps more importantly, no Intervenor took issue with the appropriateness and quantum of the Garland settlement. There is no issue about the Company's actions in settling this lawsuit in 2006.

## B. Factual basis for recovery

11. The amounts in the CASDA represent the defence and settlement costs associated with the class action lawsuit commenced by Gordon Garland against the Company in 1994. Mr. Garland's lawsuit attacked the LPPs charged by the Company on the basis that, in certain circumstances, the effective annual interest rate associated with the LPP could exceed the legal limit. The LPPs were approved by the Board and were a component of the Board's rate orders that governed the amount that the Company could charge each year for the transmission, delivery and storage of gas.

**a) the LPPs were a component of just and reasonable rates**

12. There are a number of important aspects to the LPPs at issue in the Garland proceeding that, taken together, demonstrate that it is just and reasonable that EGD be permitted full recovery of the amounts expended in their defence.

***i) EGD's LPP resulted from the implementation of Government policy***

13. In 1978, the Ontario Government convened a task force to consider how to align the myriad of billing, collection, credit and termination of service policies of Ontario's gas, electric and water utilities. The task force developed a set of voluntary guidelines titled "Residential Guidelines for Credit Collection and Cut-Off Practices of Public Utility Suppliers". The Guidelines were presented to the Legislature, at which time the Minister of Energy stated that it was his expectation that the Guidelines would be adopted by most of Ontario's public utilities, which they in fact did.[10]

***ii) EGD's LPP is part of Board rate orders***

14. The Company's proposed new form of LPP, which was in conformance with the Guidelines, was initially reviewed and approved by the Board as part of its April 2, 1980 decision in the

[10] Ex. B-2-1, pp. 1-4.

Company's E.B.R.O. 369-II rate proceeding.[11] The LPP, as approved by the Board, was a one-time charge equal to 5% of the customer's current month's gas charges (exclusive of charges for other items, such as water heaters), if the bill was not paid within 16 days of mailing.[12] EGD's LPP has been part of the Company's Board-approved rate orders for every year such orders were issued from 1981 to the present.[13]

15. As a matter of law, the Company is not permitted to charge for the distribution and sale of natural gas, except in accordance with Board-approved rate orders.[14] The Board considers each rate or charge and, if appropriate, finds that the rate or charge is just and reasonable. The definition of "rate" in the Act includes "a penalty for late payment".[15] Accordingly, the LPPs were a part of the just and reasonable rates approved by the Board each year. Once a final rate order is issued, the Company is required to ensure that its charges are consistent with the provisions of those rate orders. Indeed, if the Company fails to abide by its rate orders, it faces the prospect of sanctions, including substantial fines.[16] Accordingly, the Company was required to implement and charge its LPP, as soon as the rate orders including the LPP became effective.[17]

***iii) LPPs generally supported by Intervenors***

16. In each rate case proceeding, it has been open for Intervenors, representing different constituencies of customers and other stakeholders, and for Board Staff, representing the public interest, to challenge any aspect of the Company's filing. Since 1981, the Company has included the LPP as part of the rates for which it seeks approval. The Company's prefiled evidence in each of its rate cases from 1994[18] to 2002[19] indicated that "[The Company] will continue to apply the late payment penalty as a means of ensuring that all customers pay promptly so as to minimize the costs of carrying and collecting accounts that must be borne by all customers in rates charged for the sale of natural gas".[20] The Company's LPP was

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[11] Ex. B-2-1, p.3 and Ex. C-1-3.
[12] Ex. B-2-1, pp. 5 and 7.
[13] Ex. B-2-1, pp. 4-5.
[14] OEB Act, s. 36(1) (similar provisions existed in the predecessor legislation).
[15] OEB Act, s. 3.
[16] OEB Act, s. 112.1-112.5 and 126 (similar provisions existed in the predecessor legislation).
[17] Ex. B-2-1, p. 5.
[18] When the Garland proceeding was initiated.
[19] When the Company's LPP was changed.
[20] Ex. B-2-5, pp. 1-3 and Ex. C-1-29.

presented and approved each year, generally without debate and often as part of a settlement agreement with all interested stakeholders.[21]

17. To the best of EGD's knowledge, until 2001 when the Board instituted a process to change utility LPPs, no party ever challenged the LPP on the basis that it might contravene the legal limit on interest. In fact, the Company is only aware of one challenge to its LPP, which was unsuccessful.[22] Specifically, in the E.B.R.O. 452 proceeding (1989 rate case), one of the Company's customers (Julius C. Olsen) objected to the LPP and said that it became effective too quickly, as compared to other late payment penalties for credit cards, and that it should be based on a commercial interest rate.[23] There is no evidence from the Board's Decision with Reasons in E.B.R.O. 452 (or any Intervenor's argument) that any other party supported Mr. Olsen's position. It bears note that, as part of its submissions in the E.B.R.O. 452 proceeding, EGD invited the Board to re-examine all issues related to the LPP, if that was deemed appropriate. In response to the customer's complaint and the Company's submissions, the Board's Decision expressly approved the Company's continued use of the LPP, stating that:

> In the Board's opinion, it must be emphasized that the guidelines proposed by the Ontario government in 1978, though minimal, were optional guidelines**. In the Board's view, the Company can hardly be criticized for voluntarily adopting and adhering to the Government's own guidelines, in respect to both the time allowed for payment and the penalty.**
>
> The Board takes the position that the guidelines ought to be followed unless there is good reason to change them. … The Company's late payment policy will remain unchanged.[24] [emphasis added]

***iv) LPPs intended for ratepayer benefit and did benefit ratepayers***

18. The LPP is intended to, and does, protect ratepayers, by acting as an encouragement to pay accounts in a timely manner.[25] When that happens, the Company's recoverable costs for working cash requirements and bad debt exposure, as well as administrative costs, are reduced.[26] In addition, the forecast LPP revenues are credited as an offset to the Company's revenue requirement. As a result, the inclusion of LPPs as part of the Company's rates

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[21] Ex. B-2-5, pp. 1-3.
[22] Similarly, as detailed in the Company's prefiled evidence, and in the argument filed by Union, the Board considered and dismissed a challenge to Union's LPP in rate cases in the late 1980s: Ex. B-2-1, p. 8 and C-1-6 and Union Argument, paras. 25-27.
[23] Ex. B-2-1, pp. 5-7.
[24] Ex. C-1-5, pp. 11-12.
[25] Ex. B-1-1, p. 6.
[26] Ex. B-1-1, p. 2 and Ex. C-1-16, pp. 4 and 15.

operates to reduce the revenue requirement, and hence rates. Forecast LPP revenue is allocated and credited to ratepayers on the basis of customer numbers (meaning that all customers receive equal benefit).[27] With the LPP, the bad debt and working cash costs that are part of the Company's revenue requirement are also reduced, leading to lower rates. On the other hand, the LPP is not designed to increase the Company's shareholder's return, since the amount that is forecast as LPP revenues directly reduces the amount that the Company can recover in distribution rates.[28]

19. Accordingly, ratepayers benefited from the existence and use of the LPP because rates were lower over the relevant period than they otherwise would have been without the LPP and because the LPP discouraged late payers.[29]

**b) EGD took the proper approach to the Garland litigation and changing the LPP**

20. The evidence demonstrates that the Company acted in good faith, and appropriately, throughout the period subsequent to the commencement of the Garland litigation. The Company took all reasonable steps to avoid and minimize exposure in the litigation, and followed the direction of the Board and the Courts in implementing a new LPP at the appropriate time.

***i) EGD fought liability and won at most levels***

21. Upon receipt of the Garland Statement of Claim in 1994, the Company took the position that the LPP was valid and moved to vigorously defend the action.[30] Up until the time that the Supreme Court of Canada issued its first decision in October 1998, no participant in OEB proceedings expressed any disagreement with the Company's position that, as set out in its Statement of Defence, the LPP was not subject to the provisions of section 347 of the *Criminal Code*. An experienced and respected jurist (now Ontario's Chief Justice) from the Ontario Court (General Division) and three judges of the Ontario Court of Appeal agreed. Accordingly, there appeared to be no compelling reason to seek to change the LPP. [31] It was also recognized that to change the LPP in 1994 had attendant litigation risks in that this might

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[27] Ex. B-2-1, p. 4.
[28] To put it another way, had the LPP been set at a lower level, then distribution rates would have been set higher, in order to allow the Company to recover its full revenue requirement.
[29] Ex. B-2-6, p. 3.
[30] Ex. B-2-2, p. 1.
[31] Ex. B-2-3, p. 1.

validate or give weight to Mr. Garland's complaints.[32] Moreover, there was a prospect that changing the LPP would lead to an increase in distribution rates, because of a reduction in offsetting LPP revenues. Neither the Board, nor any Intervenor, opposed EGD's approach.

22. Even after the first Supreme Court of Canada decision, many defences remained open to EGD to justify the continued application of the LPP. Indeed, EGD succeeded in some of these defences as Mr. Garland's action was again dismissed by the Ontario Superior Court in 2000, and this dismissal was upheld by the Ontario Court of Appeal in 2001.[33]

23. It would appear that ratepayers did not disagree with the Company's course of action in fully defending the action, given that the continuance of the CASDA, and the recovery of the Company's defence costs that were collected in the CASDA, were the subject of settlement agreements in five different rate cases.[34]

***ii) The LPP was changed at the appropriate time***

24. Following the Supreme Court of Canada's October 1998 decision, it became apparent that the OEB did not wish to address whether the LPPs being used by Ontario utilities should be changed until after the Ontario Court had re-heard the matter and come to a decision. Specifically, on November 30, 1998, the Board stated:

> Another matter requires comment from the Board. The Board has noted the Supreme Court of Canada's recent decision in Garland vs. Consumers Gas, a decision concerning the late payment penalty provisions of that utility. The Supreme Court has referred the matter back to the Ontario Court (General Division) for determination on the facts of the case. Given the similarity between the late payment provisions of Union Gas and the one under consideration by the Court, the Board wishes to inform the Company [Union] and intervenors that the Board does not intend, on its own motion, to address this matter in EBRO 499.
>
> Rather, the Board will await the Court's determination on this matter before addressing the current late payment penalty provisions of Union and Enbridge Consumers Gas.[35]

25. The Ontario Superior Court of Justice subsequently (in April 2000) dismissed Mr. Garland's claim and found that the OEB was the appropriate forum to address issues related to the LPP.

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[32] Ex. B-2-3, p. 1.
[33] Ex. B-2-2, p. 3 and Ex. C-1-9.
[34] Ex. B-2-5, pp. 1-3: RP-1999-001 (Ex. C-1-29, p. 18), RP-2000-0040 (Ex. C-1-29, p. 24), RP-2001-0032 (Ex. C-1-29, p. 28), RP-2002-0133 (Ex. C-1-29, p. 67) and RP-2003-0048 (Ex. C-1-29, p. 79).
[35] Ex. B-2-3, pp. 1-2 and Ex. C-1-14.

26. On January 30, 2001, while most utilities in Ontario still employed an LPP similar to EGD's, the OEB issued a Notice indicating that it was appropriate "at this time" for the Board to review its policy with respect to the setting of LPPs.[36] On April 4, 2001, Board Staff issued a discussion paper titled "Electricity & Gas Distributor Late Payment Charge Policy", "to solicit input from stakeholders on various options for electricity and gas distributor late payment penalty".[37] Many parties submitted comments in response to the Board Staff discussion paper. One of the common concerns expressed in the comments was that changes to the LPP would result in increased rates for all customers. No Intervenor took the position that the conduct of utilities (including EGD) or the Board's approval of the LPP up to that time had been misguided or inappropriate.[38] Indeed, VECC noted that:

> [a]s these charges come about as a result of obligations sanctioned by the Board's rate and rule making authority, it is a dubious proposition to suggest that the establishment of a late payment policy is part of the prerogatives of distributor management.[39]

27. VECC expanded on the above comment in its argument in this case, noting that:

> [t]he issue raised by the VECC submission relates to a concern … that individual distributors create their own LPP policies. It was VECC's position that the issue of an appropriate LPP policy was of such importance that the Board should exercise its jurisdiction to set a uniform, fair, transparent, simple and symmetric LPP policy through proper consultation with all stakeholders on all relevant issues.[40]

28. These comments confirm the fact that EGD was never in a position to unilaterally implement a new LPP. The process would have required the involvement of the Board and all stakeholders.

29. In October 2001, after reviewing the recommendations of Board Staff, and the submissions of stakeholders in response, the Board directed gas and electricity distributors to implement a new form of LPP.[41] In December 2001, the Ontario Court of Appeal released its second decision which stated that while it was now time to change the LPP, it was appropriate for the Board to have waited for the Court to address the issues in the Garland proceeding before requiring changes to the LPP.[42] Shortly thereafter, with the Board's approval, the Company changed its LPP. Effective February 1, 2002, the Company's LPP was reduced to a one time

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[36] Ex. B-2-3, p. 2.
[37] Ex. C-1-15.
[38] Ex. B-2-3, p. 3 and Ex. C-1-15 and Ex. C-1-16.
[39] Ex. C-1-16, p. 29.
[40] VECC Argument, para. 48.
[41] Ex. B-2-3, pp. 4-5 and Ex. C-1-17.
[42] Ex. B-2-3, p. 5 and Ex. C-1-10, p. 16.

2% charge.[43] The new form of LPP was considered to be compliant with legal limits on interest rates.

***iii) The Company appropriately responded to the SCC's second decision***

30. In April 2004, more than two years after EGD's LPP was changed, the Supreme Court of Canada issued its second decision. In that decision, the Court ruled that EGD was liable to refund any LPP amounts paid by Mr. Garland in excess of the legal limit, and returned the matter to the Ontario Court for determination of issues related to certification of the class action and determination of the level of damages, if any.[44] The Supreme Court's second decision did not contain any direction to the Board about the recoverability in rates of any costs or judgments associated with the case.

31. The Company then entered into mediation and settlement discussions that ultimately resulted in the Court-approved settlement of the case, before any specific determinations were made about the Company's liability. No party in this case disputes the appropriateness and reasonableness of the settlement that was ultimately approved by the Court.

**c) The amounts in the CASDA are prudently incurred costs**

32. The amounts in the CASDA are the current costs incurred by the Company in defending and resolving the Garland litigation in 2006. The balance in the CASDA is comprised of three elements: (i) EGD's remaining legal, expert and other defence costs; (ii) the settlement payment; and (iii) interest.

33. By far the largest element of the CASDA account is the $22 million settlement payment that was made to resolve all issues in the Garland proceeding. The reasons why this settlement was fair and appropriate in the circumstances of this case, and represents good value for the Company and its ratepayers, are set out in detail in the Company's prefiled evidence.[45] No party has challenged or put in issue the amount of the settlement – VECC specifically noted that it does not object to the quantum of the settlement insofar as it was reviewed and approved by the Ontario Superior Court of Justice.[46] It is important to note that a large portion

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[43] Ex. B-2-3, pp. 5-6 and Ex. C-1-20.
[44] Ex. B-2-2, p. 4 and Ex. C-1-11.
[45] See especially Ex. B-2-4.
[46] VECC Argument, para. 12; CCC noted that it has no basis on which to challenge the reasonableness of the ultimate settlement of the Garland Action: CCC Argument, para. 29.

of the settlement will benefit the Company's most vulnerable ratepayers for years to come.[47] The $9 million endowment to the Winter Warmth Fund ("WWF") will ensure that there is substantial funding for the WWF's activities for the foreseeable future.[48]

34. The defence costs included in the CASDA relate to the legal, actuarial, consulting and expert activities undertaken to assist the Company in the defence and settlement of the action.[49] These defence costs have accrued since the CASDA was last cleared as part of the Company's F2004 rate case. The defence costs included in the CASDA were cleared to rates on six occasions between 1994 and 2004, most times as a result of settlements between the Company and all Intervenors.[50] Thus, until the second Supreme Court of Canada decision, there appears to have been no principled objection to the recovery of the Company's defence costs.

35. While there are certainly many points of similarity between this case and the class action suits still faced by Union and electricity distributors, it is important to note that the amount that EGD seeks to recover from the CASDA is unique to this case. As Union states in its argument, "the quantum of recoverable costs associated with LPP litigation costs must clearly be evaluated on a case by case basis".[51] The Garland case involved very protracted litigation and addressed and resolved many legal issues that will be instructive or determinative in the other similar proceedings. The Garland proceeding was the test case for each of these suits and it may be expected, therefore, that the legal (and potentially settlement or judgment) costs associated with this case may exceed the others. The evaluation of the amounts in the CASDA is appropriately viewed from that perspective.

**d) EGD's proposal for the clearance of the CASDA is fair and appropriate**

36. The Company requests that the actual amount recorded in the CASDA as of the date of the decision in this proceeding, including interest, be cleared to ratepayers in equal amounts over a five or eight year period beginning in 2008. The Company's original proposal was for clearance over eight years, but the Company also supports CCC's submission that recovery could

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[47] In this regard, it is interesting to note that VECC, whose constituents would presumably benefit most from the endowment, object to the Company's Application while CCC, whose constituents would presumably benefit less (on average), does not object.
[48] Ex. B-2-4, pp. 5-7.
[49] Ex. B-2-5, p. 4.
[50] Ex. B-2-5, pp. 1-3.
[51] Union Argument, para. 3.

properly be effected over the five year incentive regulation term.[52] Spreading the recovery over several years will avoid the possibility of rate shock impacts. The Company requests that interest continue to accrue, in the ordinary fashion, on the remaining balance in the CASDA until it is fully cleared.[53]

37. The Company proposes that the recovery of the CASDA from ratepayers through annual clearances be allocated in the same manner as LPP revenues were credited to ratepayers in relevant years. Specifically, it is proposed that the allocation of the recovery of the CASDA be done on the basis of the number of customers in each class, which is the methodology that the Company used to allocate late payment revenues to the rate classes in the Board-approved fully allocated cost study.[54] No party disagrees with this proposed approach.

38. Under the Company's proposal, the balance in the CASDA, including accrued interest, will be cleared in equal amounts over several years, beginning in 2008, at the same time as deferral and variance accounts are cleared each year. The combined clearance would appear as a one-time adjustment each year on the customers' bills. For each year's clearance, the Company will allocate the amount to be cleared to the rate classes based on the number of customers in each rate class in that year.[55]

39. In general terms, recovery over eight years equates to less than $2 per year per customer, and recovery over five years equates to approximately $2.70 per year per customer. Given that the vast majority of the Company's customers are in Rate 1, most of the recovery will come from that rate class.[56] On the other hand, some of the smaller rate classes (Rates 100 and above) will experience almost no impact from the proposal.[57]

## C. Legal basis for recovery

40. The amounts in the CASDA are current costs, prudently incurred in the course of carrying on business, that have been collected in a deferral account for disposition at the appropriate time. As seen in the following discussion, the Company respectfully submits that, in accordance with

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[52] CCC Argument, para. 28.
[53] Ex. B-2-6, p. 1.
[54] Ex. B-2-6, pp. 1-2 and response to SEC Interrogatory #1.
[55] Ex. B-2-6, p. 2.
[56] *Ibid*.
[57] Indeed, the *aggregate* impact of the proposal on all Ontario members of IGUA combined will be in the range of $1000 (or $13.50 per customer).

applicable legal tests, it is fair and appropriate that it be permitted full recovery of all amounts in the CASDA.

**a) The expenses contained in the CASDA were prudently incurred**

41. It is well-established that a utility is entitled to recover its prudently incurred costs.[58] When those costs are collected in a deferral or variance account, then the prudence determination takes place at the time that the applicant seeks to clear the account.

42. Notwithstanding the fact that Union filed argument in this case in advance of other Intervenors, setting out the prudence standard and the reasons why the amounts recorded in the CASDA were prudently incurred, only one Intervenor (IGUA) specifically raised the prudence issue in argument and even then, only in one sentence. No party has questioned, in any way, the prudence of any particular item or cost contained in the CASDA. IGUA submitted simply that charging the impugned LPP was a "wrongful act", so it could not be characterized as prudent.[59] With respect, leaving aside EGD's rejection of the position taken by IGUA (which is addressed below), this position completely ignores the fact that a prudence review is to be conducted in light of the information available at the time that decisions were made.[60] Amounts in the CASDA relate to the defence of the Company's observance of historical rate orders. Up until February 2002, when the LPP was changed, there was no determination of liability by EGD to Mr. Garland, and the legal issues related to the LPP were very much unresolved. Indeed, the Ontario Court of Appeal stated in December 2001 that the OEB had "quite properly" waited until that time to address changes to the LPP. If it was appropriate for the regulator to have waited until then, surely then it was appropriate for EGD to have continued to obey and apply the regulator's rate orders.

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[58] *Enbridge Gas Distribution Inc.* v. *Ontario Energy Board*, 2005 CanLII 4941 (Ont. Div. Ct.), at para. 8, citing (among other cases) *State of Missouri ex. rel. Southwestern Bell Telephone Co. v. Public Service Commission of Missouri*, 262 U.S. 276 (1923) at 289; *British Columbia Electric Railway Co. Ltd. v. British Columbia (Utilities Commission)*, [1960] S.C.R. 837 at 854; and *Transcanada Pipelines Ltd. v. Canada (National Energy Board)*, [2004] F.C.J. No. 654 (C.A.) at para. 32; see also C.F. Phillips, The Regulation of Public Utilities (Arlington, Public Utilities Reports, 1993), pp. 255-258.

[59] IGUA Argument, p. 2.

[60] As stated by the Board in EGD's F2002 rate case, "To be prudent, a decision must have been reasonable under the circumstances that were known or ought to have been known to the utility at the time the decision was made" and "Hindsight should not be used in determining prudence, although consideration of the outcome of the decision may legitimately be used to overcome the presumption of prudence.": EB-2001-0032, paras. 3.12.1 to 3.12.5; this test was confirmed in *Enbridge Gas Distribution Inc.* v. *Ontario Energy Board*, 2005 CanLII 4941 (Ont. Div. Ct.) and 2006 CanLII 10734 (Ont. C.A.), paras. 8 to 11.

43. Where activities are carried out, in good faith, for the benefit of a utility's ratepayers, and are later challenged in litigation, then it is appropriate that the costs (including any judgment) of the utility's defense of those activities (whether successful or not) be recovered from ratepayers. This is particularly so when the activities in question are the implementation of aspects of rate orders approved by the utility's regulator, and where the relevant aspects of the rate orders actually benefited ratepayers by reducing rates. A utility's litigation costs, where its conduct is challenged, are no different in character from other costs of operation. The costs of a judgment are indivisible from the defence costs incurred – both are costs incurred to respond to challenges to the utility's activities. As noted by Union in its argument, there is ample precedent, particularly in American cases, for the proposition that a utility is entitled to recover its costs for activities undertaken for the benefit of ratepayers, even where those costs involve subsequent litigation challenging the propriety of the activities.[61]

**b) The allocation proposal is just and reasonable**

44. In addition to the question of whether the expenses contained in a deferral account were prudently incurred, and should be recovered, the OEB must also determine how the amounts are to be recovered from ratepayers, including "the appropriate number of billing periods over which the amount shall be divided in order to mitigate the impact on consumers".[62]

45. The Company submits that its proposal in this case is fair from a cost causality perspective. It provides that recovery is to be implemented using the same allocation principles that applied for the credit of LPP revenues to ratepayers. No party has objected to this aspect of EGD's proposal. The proposal is also fair from a rate impact perspective because recovery over a lengthy period ensures that there is, as noted by Board Staff, a "very low monetary impact" on an annual basis.[63]

46. VECC submits in its argument that it is premature for the Board to address "implementation issues" at this time.[64] EGD respectfully submits that the Board has all the information necessary to make a decision at this time, and there is no need for further stages or phases of

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[61] Union Argument, at pp. 13 to 16 citing several cases, including *Mountain States Telephone and Telegraph Company* v. *FCC*, 939 F.2d 1035 (U.S. Court of Appeals, D.C. Cir., 1991); see also *Iroquois Gas Transmission System* v. *FERC*, 145 F.3d 398 (U.S. Court of Appeals, D.C. Cir., 1998).
[62] OEB Act, s. 36(4.5).
[63] Board Staff Submissions, p. 2.
[64] VECC Argument, paras. 39 to 41.

this proceeding. Indeed, it is difficult to contemplate what additional information could be generated or produced to render a decision.

**c) Response to Board Staff request for comments**

47. At the end of its submissions, Board Staff asked parties to address a number of items related to the proposed 8 year recovery of the amounts recorded in CASDA. Specifically, Board Staff asked about the impact of effecting the recovery over a shorter period, in terms of customer impact and interest cost savings. Set out below is a chart, setting the dollar impact of recovery over shorter numbers of years.

| Number of years for recovery | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|---|---|---|---|---|---|---|---|---|
| Principal amount to be recovered[1] | 23,545,001.28 | 23,545,001.28 | 23,545,001.28 | 23,545,001.28 | 23,545,001.28 | 23,545,001.28 | 23,545,001.28 | 23,545,001.28 |
| Interest amount to be recovered[2] | 1,705,409.78 | 2,290,797.32 | 2,846,165.09 | 3,394,027.78 | 3,938,888.60 | 4,482,248.31 | 5,024,750.43 | 5,566,716.36 |
| Total amount of recovery | 25,250,411.06 | 25,835,798.60 | 26,391,166.37 | 26,939,029.06 | 27,483,889.88 | 28,027,249.59 | 28,569,751.71 | 29,111,717.64 |
| Total annual amount of recovery | 25,250,411.06 | 12,917,899.30 | 8,797,055.46 | 6,734,757.27 | 5,496,777.98 | 4,671,208.27 | 4,081,393.10 | 3,638,964.71 |
| Annual cost per customer[3] | 13.50 | 6.80 | 4.50 | 3.40 | 2.70 | 2.30 | 1.90 | 1.70 |

48. EGD submits that recovery over eight years is an appropriate approach; however, it also understands the administrative simplicity of CCC's alternate approach[65] of aligning the recovery with the term of EGD's incentive regulation plan, over the five years from 2008 to 2012. EGD also supports that approach.

## D. Reply

49. This Argument now turns to the specific arguments raised by Intervenors. For the sake of expediency, the Company has combined its response to Intervenors' arguments under the following general headings.

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[65] CCC Argument, para. 28.

**a) EGD's conduct was appropriate**

50. Each of IGUA, SEC and VECC submit, in effect, that because the Supreme Court of Canada found that some of the LPPs paid subsequent to the Garland Statement of Claim being served in 1994 *may have* exceeded permissible levels, all of the amounts paid to settle the Garland class action suit should not be recoverable in rates. The implication of these submissions is that EGD could have done something after receiving the Garland Statement of Claim in 1994, and the alleged failure to take action is justification for non-recovery. This submission has no basis in fact or law. There are numerous reasons why this is so.

51. At the outset, it should be noted that there has been no judicial finding that any amount paid as an LPP exceeded permitted levels of interest. While the Company accepts that some exposure existed, issues remained unresolved as to when interest starts accruing on unpaid accounts, what amounts were to be considered as principal and to what extent interest had to be refunded. All of this would have had a significant impact on the extent to which the amounts paid exceeded the permitted maximum.[66] There is, therefore, no finding that EGD received a payment in excess of the legal limit or that any "actionable tort"[67] has been committed.

52. In any event, regardless of whether any portion of the LPP exceeded permissible limits, any change to it required approval from the OEB. Until approval for change was received, EGD could not have altered the LPP. In response to those Intervenors that implicitly take the position that recovery should be denied because the actions of the Company in respect of the LPP were in effect imprudent, the Company submits that Intervenors have failed to "drill down" to consider, specifically, the options available to the Company at relevant times for the purposes of evaluating the prudence of what the Company actually did as against the options available. Looking at circumstances at the time when decisions were made is, of course, the approach that is to be taken in evaluating prudence. Hindsight is not to be used.

53. Reduced to its simplest terms, Intervenors imply that the decision to vigorously defend the Garland lawsuit and the LPP, rather than immediately seeking to change the LPP, was an imprudent decision. Intervenors fail to consider the perception and the precedent that would be set where a utility responds to a Statement of Claim, considered meritless, by acceding to the

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[66] Ex. B-2-4, pp. 15-16.
[67] As alleged by IGUA at p. 2 of its Argument.

claimant's demands. Such a response would surely have emboldened Mr. Garland, making settlement less likely[68] or more costly in future, and would encourage similar claims in future.

54. In support of this position, Intervenors offer nothing in the way of evidence which was available at relevant times which would have caused EGD, other utilities, Intervenors, or the Board any cause for concern about the continuance of the LPP. In fact, the Garland lawsuit raised a large number of novel and difficult legal issues, and it is entirely reasonable to assume that Intervenors expected the Company to fully defend and litigate these issues, in an effort to avoid liability.[69] Indeed, one can assume that Intervenors would have argued imprudence on the Company's part had not it acted precisely as it did. As noted by CCC in its Argument[70], the difficulty with this line of the Intervenors' argument is that it requires a finding by the Board "that EGD would have had to assumed, at the moment that the Garland action was commenced, that the essential argument of the Garland action was correct." Because there was no factual basis to so conclude at the time, CCC agrees with the Company that it was reasonable for EGD to have defended the Garland action. In other words, on the basis of the record, CCC agrees that EGD's actions were prudent.

55. The defence of the Garland lawsuit was not undertaken clandestinely by EGD. On the contrary, the Board and Intervenors were kept fully apprised of the nature of the claim and the steps taken by the Company to defend the lawsuit. Intervenors were fully cognizant of the assertions being made by Mr. Garland in respect of the LPP to the effect that it was contrary to the *Criminal Code.* If Intervenors believed that the LPP was in any way unlawful or that the Garland lawsuit had merit, Intervenors could have commented on the continuance of the LPP, suggested an alternative, or asked the Board to impose changes. Intervenors could also have appealed the rate orders that approved the LPP. The fact is that none did. To the contrary, EGD's legal fees and disbursements incurred defending the Garland lawsuit were cleared to rates on numerous occasions with the support of Intervenors. At a minimum, this suggests that parties supported, or did not oppose, the Company's vigorous defence of the Garland lawsuit and by association, the continuance of the LPP. The Company submits that the conduct of

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[68] Among other things, this would have opened up the potential for liability from 1981 on, as set out in the Statement of Claim.
[69] Of course, the Company was successful in many of its defences through many of the rounds of this protracted litigation.
[70] CCC Argument, p. 5

Intervenors supports a finding by the Board that Intervenors were similarly of the view that the Garland lawsuit was meritless and that there was little expectation of liability.

56. The weakness of the Intervenors' position becomes fully apparent when one considers the combined impact of what is being submitted. In short, Intervenors are saying the Company should be penalized now for failing to do something in 1994, which it could not do without Board approval, which action likely would have been opposed at the time by Intervenors given the impact on the revenue requirement and rates, and which would have negatively affected the Company's response to the Garland lawsuit, perhaps making it more costly to ultimately settle. To now impose on the shareholder a penalty under such circumstances is clearly unwarranted.

57. Finally, EGD expresses concern about the apparent implications of IGUA's suggestion that "wrongful acts were countenanced by the regulator and the Province of Ontario". This is an unfortunate mischaracterization of what occurred. To suggest, as the term countenance means[71], that the regulator and the Province approved, favoured, or encouraged wrongful acts is absurd given the commitment by both to protect the public interest and the underlying goal of the LPP to minimize the carrying and administrative costs imposed by delinquent ratepayers on those that pay on a timely basis.

58. While EGD does not believe that any party or institution should be blamed or found at fault, IGUA's comments demand a response. It is noteworthy that the only parties not branded as culpable by IGUA are ratepayer groups who participated in matters throughout. To the extent that blame exists anywhere, customer representatives are no less culpable given their failure to raise any issue about the continued imposition of the LPP, all the while members of these ratepayer groups continued to benefit from the revenue requirement implications of the LPP continuing unchanged. A fair observer would acknowledge that a regulator undoubtedly places reliance upon ratepayer groups to have fully considered the foreseeable implications of a proposed rate or charge and that while ratepayers groups will represent their constituents' best interests, no ratepayer group will be a signatory to a settlement proposal approving any rate or charge that they believe to be unlawful.

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[71] Random House College Dictionary (New York, Random House Inc. 1984), p. 306.

**b) Forecast risk**

59. Several Intervenors attempt to characterize the recovery sought by the Company as an adjustment to forecasts of LPP revenue made by the Company in prior years. The suggestion is then made that EGD bears the risk of inaccurate forecasts.[72] While it is true that the Company does bear forecast risk in the ordinary situation of forward test year ratemaking, that principle has no application here.

60. The "CASDA litigation" is not, as SEC argues, analogous to a variation in any cost or revenue item".[73] As is clear from the pre-filed evidence, the recovery sought has nothing to do with the forecast of LPP revenues at any time, and instead has to do with the current costs of resolving litigation based on the nature of historic Board-approved LPPs.

61. EGD's position in this regard is supported by CCC. In its Argument, CCC noted that it "does not believe that the circumstances of this case can properly be branded as a forecasting error. It was not the accuracy of the forecasts that was in issue, but rather whether the formula on which they were based was legal." [74]

**c) EGD's return on equity ("ROE")**

62. IGUA uniquely brands the amounts which the Company seeks to recover in this application as "uninsured litigation damages and costs" and then conveniently argues that this is a risk for which the Company is compensated through the equity risk premium component of its ROE.[75]

63. Even if the Board were to accept IGUA's novel submissions in respect of uninsured losses, it is clear that the amounts for which recovery is sought in this Application are not a foreseeable business risk, and do not fall within the category of risks for which a utility's ROE compensates. Indeed, if ROE were meant to cover this type of risk, then the Board-approved level would have to be increased.[76] It is unimaginable that any person, let alone a sophisticated utility investor, would anticipate that costs arising out of the defence and settlement of a lawsuit against a

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[72] Both SEC and VECC tie this argument to their interpretation of the "regulatory compact" (SEC Argument, para. 12 and VECC Argument, paras. 24-38). What each Intervenor fails to address, however, is the reality that a fundamental premise of any "regulatory compact" that might exist is that a utility will only charge its customers in accordance with rates that have been filed and approved by its regulator.
[73] SEC Argument, para. 16.
[74] CCC Argument, p. 4.
[75] IGUA Argument, p. 2.
[76] CCC agrees with this position, at p. 5 of its Argument.

utility for the consequences of having implemented and complied with its regulator's orders would not be recoverable in rates. Stated differently, no one would ever have thought that one aspect of legitimate regulatory risk would be the risk of non-recovery of a cost that was incurred as a result of the good faith compliance with Board orders implemented by the utility for the benefit of ratepayers.

64. IGUA continues in its argument stating "the Board will know" the extent to which "business risk" is covered by the ROE.[77] Implicit in this submission is the fact that IGUA cannot point to any Board decision or guideline to support its proposition and accordingly, IGUA is relegated to wishfully urging the Board to adopt novel concepts and terms like the risk of "uninsured litigation losses". The implication that only the Board is aware of what is a component of the equity risk premium is inaccurate and contrary to the Board's goal of establishing a formulaic approach to the development of a return on common equity for regulated utilities. Indeed, the Board has stated that an advantage of moving to and using formula-based allowed equity returns is that it is more readily understood by all participants and helps ensure consistency.[78]

65. Of note is the fact that IGUA makes no reference to the Board's draft Guidelines on a Formula-Based Return on Common Equity for Regulated Utilities, dated March 1997 (the "ROE Guideline"). The OEB adopted a formula-based approach using the equity risk premium method for the determination of a fair return on common equity.[79] The factors which the Board enumerated as being relevant for the purposes of establishing an equity risk premium include the relationship between interest rates and the implied risk premium, the need to adjust "bare bones" ROE for financing flexibility and the riskiness of equity relative to long Canada bonds and the overall stock market.[80]

66. Without accepting that IGUA has properly characterized the recovery sought in this application as being an "uninsured loss", it is noteworthy that there is no reference to such risk in the ROE Guideline nor, to the Company's knowledge, has a risk of uninsured losses ever been identified

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[77] *Ibid*, p. 3.
[78] OEB's draft Guidelines on a Formula-Based Return on Common Equity for Regulated Utilities, dated March 1997, p. 7 (http://www.oeb.gov.on.ca/documents/cases/RP-1999-0034/PO3APPA.PDF) ; see also Dr. William T. Cannon, "A discussion paper on the determination of return on equity and return on rate base for electricity distribution utilities in Ontario", December 1998, p. 33 (http://www.oeb.gov.on.ca/documents/cases/RP-1999-0034/ROEfinal3.pdf ) .
[79] ROE Guideline, pp. 28-32.
[80] ROE Guideline, p. 30.

as a component of the equity risk premium. There is certainly no support in the ROE Guideline for IGUA's notion that 100 basis points of the equity risk premium relate to "uninsured litigation losses".[81] On the contrary, the foundation of rate-making and a pre-requisite to a fair ROE is that a utility be permitted to recover all costs prudently incurred to provide service. Not all costs of service are insurable and neither the existence of insurance nor the insurability of a cost enters into the test to determine whether the cost was reasonably incurred in respect of the delivery of a utility service. If it was, the cost should be recoverable in rates. Accordingly, IGUA is attempting to introduce an entirely new concept into rate regulation, totally unsupported by any regulatory or judicial precedent, text or scholarly work.

67. The punitive consequences of what IGUA proposes are masked by its erroneous description of how a denial of recovery would be booked. IGUA argues, without any support, that a disallowance of amounts in the CASDA would operate as a reduction of the Company's equity capital.[82] That is not the case. Any disallowance will result in an equal and immediate reduction in the Company's earnings in the year the disallowance is incurred. There is absolutely no basis to assume that such a reduction in earnings would, as IGUA suggests[83], be absorbed without difficulty. Indeed, if IGUA's position was accepted, and the Company was disallowed recovery of the CASDA, this would result in an equal and immediate reduction of the Company's overall earnings, and would likely impact on its ability to raise capital. This is certainly not consistent with the purpose and intent of the Guideline, and such a punitive approach is completely inconsistent with the circumstances of this case where the Company took all reasonable steps to avoid and minimize exposure for its ratepayers.

**d) Costs at issue are current costs**

68. A number of Intervenors have tried to characterize EGD's request for rate recovery of the LPP litigation costs as "retroactive." This characterization is wrong. The CASDA is a deferral account which contains current costs predominantly consisting of the settlement monies paid in late 2006 to settle the Garland lawsuit. As defence costs incurred prior to 2004 have already been cleared through to rates, EGD's remaining defence costs relate only to the period 2004 to

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[81] Like the 100 basis points of the equity risk premium, IGUA similarly fails to explain how or why 1% of a utility's equity capital should be used as a guide for measuring the non-recoverable portion of uninsured litigation losses as if the utility's equity capital bears any relation to defense costs and prudent settlement costs.
[82] IGUA Argument, p.2.
[83] *Ibid*.

date. Accordingly, both these costs and the costs of settlement are *current* costs which result from a lawsuit initiated against the Company in the Superior Court of Ontario, in response to which the Company determined that the most prudent course of action was to settle the proceeding in 2006, rather than to proceed to trial on a later date.

69. In its partial decision in the Company's 2004 rate case, the Board considered a request to expand the scope of the CASDA to include defence *and* judgment costs. Intervenors opposed the Company's request in this regard. The Board determined that this request was "premature" because there had been no settlement or judgment at that time and there was no likelihood that judgment amounts "[were] likely to arise in the relevant period"[84]. The Board's determination that the Company's request to expand the scope of the CASDA was premature is an acknowledgment that such costs were not yet "ripe" for consideration and were therefore not yet even current costs. At the time of the settlement, the Company provided the Board and Intervenors with an update, and it was instructed to bring this Application after the matter was finally determined by the Court.[85] As a result, the Company now seeks recovery of current costs in a deferral account set up to record such costs for future consideration by the Board.

70. For the most part, lawsuits involve disputes or claims for damages involving conduct by a party or parties that occurred in the past. So while the conduct which may be the cause of action for a lawsuit is historical, the costs to defend the proceeding are a current cost of doing business and appropriately recoverable in rates. The Company's Application for recovery of costs in the CASDA is not tied in any way to changing historical rates for which a final rate order was made. No attempt is being made to set out what rates would have been had the LPP been changed to the level approved in 2002. This Application is about recovery of current costs resulting from a prudent settlement of an ongoing dispute. Accordingly, EGD is not seeking any retroactive adjustment to its rates.

71. The result of the Intervenor position, if accepted, is that any time that a utility is involved in litigation related to its prior business activities, even where those business activities were carried out entirely for the benefit of its ratepayers, costs of that litigation would not be recoverable. That is not just or reasonable.[86]

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[84] EB-2003-0203, Partial Decision with Reasons, August 31, 2004, para. 144 (Ex. C-1-30, p. 7).
[85] Letter from OEB to EGD, dated August 17, 2006: Ex. C-1-31.
[86] See also CCC Argument, paras. 24-25.

**e) EGD should not have to further justify the amount of its defence costs**

72. While most Intervenors support, or do not oppose, EGD's recovery of its defence costs, VECC makes the suggestion that EGD should have to provide an accounting of the defence costs recorded in the CASDA *and* file a report from an independent auditor in respect of these costs.[87] With respect, EGD fails to understand the basis for VECC's position in this regard.

73. VECC lays no foundation for why it is necessary and appropriate to incur the cost of retaining an independent auditor tasked with filing a report with the Board. VECC cites no precedent nor argues that circumstances are such that the appointment of such an auditor is warranted. EGD submits that such a step is completely unnecessary and, consistent with past practice, the Board, with the assistance of Board Staff and Intervenors are in the best position to assess the prudence of such costs. EGD's puzzlement in respect of VECC's position is compounded by the fact that VECC does not question the prudence of EGD's defence, nor does VECC expressly question the quantum of such costs. VECC's concern is limited to the extent of information filed to substantiate the defence costs claimed. EGD submits there is no justification for this concern. The level of detail in this filing is consistent with that in previous applications for clearance of deferral accounts. Intervenors had the opportunity to ask interrogatories about all aspects of the Application, but chose not to do so.

74. The Board will recall that in the Company's F2007 rate case, certain Intervenors challenged the level of legal costs in another deferral account, essentially for the reason stated here by VECC that the level of detail in the pre-filed evidence was insufficient. In its Decision with Reasons, the Board allowed full recovery for the legal fees and disbursements, noting that:

> The Board does not question the Company's proposal to recover costs associated with its participation to the Ontario Court of Appeal and its application to the Supreme Court of Canada. Neither does the Board question the existence of records to support this claim. It is not expected that the Company file such detail as part of its pre-filed evidence. While the onus is on the utility to prove its case, it was open to the parties to ask for supplementary information through the interrogatory process or during the hearing when the issue was canvassed. Parties did not develop that additional record. It is not reasonable to now fault the Company for an "insufficient" record. On the record before it, the Board finds it appropriate that the recorded balance in this account should be recovered by the Company, as proposed.[88]

EGD submits that the same logic applies in this case.

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[87] VECC Argument, paras. 8 – 11.

[88] EB-2006-0034, Decision with Reasons – Phase 1, July 5, 2007, p. 54: Ex. C-1-30, p. 7.

75. In the pre-filed evidence, the Company accurately notes that the legal fees, disbursements and experts' costs for the period 1995 to 2003 have already been cleared to rates, either as a result of settlement agreements or Board decisions. Several Intervenors deny that the past clearance of such amounts is of any precedential value in this proceeding. The Company disagrees.

76. The fact that Intervenors and the Board have allowed for the clearance through to rates of the costs of the defence of the Garland action, from 1995 to 2003, supports a finding that Intervenors agree and accept the long-standing regulatory principle that a utility is entitled to recover through rates the reasonable costs incurred defending lawsuits commenced against it. The settlement agreements did not, as CCC suggests[89], contain any reservations of rights by Intervenors.[90] While VECC and SEC[91] oppose recovery of defence costs from 2005 forward, no Intervenor puts forward any principled reason why defence costs since 2005 should be treated any differently than defence costs before that time. Accordingly, the fact that Intervenors supported earlier recovery is relevant absent evidence that the remaining defence costs should be treated differently.

**f) Adjustments to the CASDA based on actual LPP revenues are not appropriate**

77. CCC's argument proposes that any rate recovery of the CASDA should be limited by the amount of any so called "over-recovery" of LPP revenue for any of the years when EGD "over-earned" during the relevant historical time period.[92] Other Intervenors also point to EGD's alleged "over-earning" during that same time period in an effort to justify their positions. There are a number of fundamental problems with this argument.

78. Most fundamentally, to clawback unforecast revenue from LPPs in the 1994 to 2002 period is retroactive rate making in its purest form. What CCC is suggesting is that recovery today of otherwise legitimate costs should be reduced by the amount of unforecast LPP revenue earned in prior historical years in respect of which final rate orders have already been made. Indeed, to effect CCC's proposal could require full comparisons, going back through 14 years of actual LPP revenues vs. forecast revenues, along with a full comparison of actual overall earnings vs.

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[89] CCC Argument, para. 10.
[90] There is no reservation of rights in the settlement agreements for RP-1999-001 (Ex. C-1-29, p. 18), RP-2000-0040 (Ex. C-1-29, p. 24), RP-2001-0032 (Ex. C-1-29, p. 28), RP-2002-0133 (Ex. C-1-29, p. 67) or RP-2003-0048 (Ex. C-1-29, p. 79) cases.
[91] SEC does not specifically address recovery in respect of defence costs, but opposes recovery generally. Thus, EGD concludes it opposes recovery of defence costs at this time.
[92] CCC Argument, para. 27.

the Board-approved return on equity, along with a re-calculation of what should have been credited for LPPs. This would clearly and unambiguously be an impermissible retroactive rate adjustment. If this proposal were allowed, Intervenors would equally be able to argue that the recovery of otherwise accurately forecast costs in a given test year should be reduced solely due to over-recovery of similar costs in a prior year.[93]

79. In any event, the premise that EGD was "over-earning" during the relevant historical time period is not supported by the evidence. If it is appropriate to look at the level of EGD's past "over-earnings" (which the Company strongly disputes), and somehow use that as the basis to now penalize the Company for any positive difference between forecast and actual LPP revenues received, then surely this must be done on an actual, and not a normalized, basis. The fact is that over the years from 1994 to 2002, EGD earned less than its allowed rate of return in just as many years (4) as it exceeded its allowed rate of return.[94] Thus, the picture painted by Intervenors of constant over-earning is misleading.

80. Moreover, an examination of the difference between forecast and actual LPP revenues would only present a partial picture of the relevant circumstances. As noted above, one of the benefits of the LPP is to reduce the incidence of late payments, which reduces the Company's bad debt expense and working cash requirements. It follows, therefore, that if the level of LPPs received by the Company in a year is greater than forecast, then the incidence of late payment is higher than forecast, and therefore the Company's actual bad debt and working cash requirements are higher than the amounts forecast for recovery in rates in that year. This will operate as an offset, such that LPP revenues in excess of forecast must be measured against the fact that the amount recovered in rates for bad debt and working cash will be too low.

81. Further, this proposal involves a significant mismatch between any historical over-recovery and the current liability for the settlement of the Garland proceeding. The settlement of the Garland case is, conceptually, restitution for amounts paid by the plaintiff that were allegedly in excess

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[93] Of course, if the rules against retroactive ratemaking are set aside, they must apply symmetrically, and in those years where the Company has under-earned because of any one of or a combination of its under-forecasting of weather, customer additions, O&M expense and other revenues, including LPP, then the Company should equally be entitled to recovery now for its past under-earnings. Aside from this being completely contrary to the purpose of developing rates on a forecast basis, allowing such an inappropriate exercise to occur would inevitably lead to a regulatory hearing death spiral. There would simply be no end to any rate proceeding, whether it be natural gas or electricity related.
[94] EB-2006-0034, Ex. I-24-45, p. 2, attached to VECC's Argument.

of the allowable interest limit. This does not match or compare to any under or over-recovery of LPPs at large, which are made up of a combination of perfectly legitimate payments which do not involve interest charges over the allowable limit and payments which may have exceeded the limit. As described in EGD's evidence, one of the reasons for the settlement was that it is impossible to accurately determine what amount of historical LPP revenue was actually attributable to interest charges in excess of the allowable limit and what portion was not.

82. It is important to note that Intervenors had the opportunity to ask EGD interrogatories in this proceeding. There is no factual foundation for the notion that EGD over-earned on LPP revenue and that this somehow materially contributed to the utility's alleged overall over-earnings in any particular historical year. No Intervenor asked for this information. Similarly, there is no information about the difference between forecast and actual bad debt expenses and working cash requirements for any particular historical years.

83. That the proposal to link recovery of the CASDA to alleged over-earning in historical years is nothing more than a penalty can be seen at least two ways. First, LPP revenues are only a small fraction of the Company's earnings in any particular year. To suggest that those revenues could ever be a driver of "over-earnings" is questionable at best. Second, in circumstances such as this where a utility acted appropriately throughout to minimize the liability that might attach to its ratepayers from the operation of past rate orders that were intended to benefit those ratepayers, it is unfair and unjust to order that the utility repay a portion of that liability out of its shareholder earnings.

**g) Intergenerational issues**

84. Several of the Intervenor arguments submit, as an argument against recovery of the CASDA, concern about alleged intergenerational inequity. With respect, this concern is misplaced. EGD's application for rate recovery of the CASDA, as discussed above, is not for a retroactive rate adjustment collected from present and future customers. The CASDA is comprised of current costs which must be paid as part of the conduct of EGD's ongoing business. The question is not whether they involve intergenerational inequity but, rather, whether they are recoverable as having been prudently incurred. The fact that part of the justification for recovery involves arguments about historical orders and customer benefits does not detract from the fact that the cost of the settlement itself is a current cost.

85. In any event, even if it were perceived that there is some element of intergenerational inequity here, because the facts underlying the Garland litigation and settlement date back several years, that concern in and of itself ought not to foreclose recovery where EGD's actions have been prudent throughout. Indeed, intergenerational issues are not uncommon and can be seen, for example, in the recent Board-approved settlement agreement related to EGD's CIS and customer care services. In that case, parties agreed to smooth costs over a five year period, even though this will result in a significant cost increase after five years because customers in the first period will receive tax benefits that are not shared by customers in the subsequent years.[95]

86. Lawsuits against any business, including utilities, are a fact of life and a foreseeable cost of carrying on business. Litigation will inevitably arise in future years alleging misconduct from the past. Companies must defend themselves and, where appropriate, settle proceedings as they are prosecuted. The unchallengeable fact is that lawsuits arising out of historic actions by a company will be defended in future years and the cost of the defence and settlement will be borne by ratepayers at that time. This "intergenerational" reality has occurred in the past and will continue. Given that past and future ratepayers have and will pay for the defence and settlement costs of actions which may have preceded their time, there is nothing unique or problematic by the request for recovery in this Application.

87. As discussed at length above, the circumstances of this case support full recovery and EGD has put forward a recovery proposal that will have a minimal impact on its customers. EGD's proposal provides that all its customers, many of whom would have been customers in the 1990s, will pay a very small annual amount for five or eight years. While it might be said that there is some degree of intergenerational impact by having the CASDA balance recovered over several years, rather than all at once, EGD submits that its proposal fairly balances those potential concerns against the adverse impact that could be felt in 2008 if the full balance were recovered in one year.

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[95] EB-2006-0034, Ex. N1-1-1, Appendix F.

## E. Summary

88. The evidence in this Application demonstrates that:

i) EGD acted in good faith in concert with the Board and Government expectations in establishing and implementing the LPP, and changing it at the appropriate time.

ii) The LPP benefited ratepayers.

iii) EGD was diligent in protecting the interest of ratepayers and itself in the Courts, by defending its use of and reliance on Board rate orders, and ratepayers did not object to the Company's approach.

iv) EGD achieved a settlement that was appropriate and prudent in the circumstances of this protracted and precedent-setting litigation.

v) The amounts in the CASDA are prudent, and essentially unchallenged by Intervenors.

vi) EGD's actions have been transparent throughout the course of the judicial process, having disclosed to the Board and regularly discussed the progress in rate proceedings with ratepayers.

89. EGD submits that, on the basis of that evidence, it is reasonable to conclude that:

i) EGD's ratepayers were the beneficiaries of the LPP and it is appropriate that they should be responsible for the prudent costs recorded in the CASDA, all of which result from the Company's defence of the LPP.

ii) It would be unfair to force the shareholders of EGD to cover the costs of this settlement when there is no evidence that shareholders derived any benefit, and given the deleterious impact that disallowance would have on annual earnings. While difficult to forecast, a reduction in earnings resulting from the disallowance proposed by Intervenors could have negative financial consequences on rates in future years.

iii) EGD has been the target of the test case in the legal battle over late payment practices in the Province of Ontario. The costs incurred by EGD that have been recorded in the CASDA will likely reduce the costs that other regulated utilities and their ratepayers may have to pay in other proceedings.

iv) The amounts recorded in the CASDA, if recovered in full by EGD over a reasonable period of time, will not impose a burden on ratepayers.

## F. Order Requested

90. EGD therefore respectfully requests that an Order be issued:

i) Approving the establishment of a 2008 CASDA, and the transfer of all amounts in the 2007 CASDA into that account.

ii) Approving the balance in the 2008 CASDA.

iii) Approving the clearance of the full balance in the 2008 CASDA, with accrued interest over time, over the course of five or eight years, in the manner set out at Exhibit B, Tab 1, Schedule 6.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 25th DAY OF JANUARY 2008**

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Dennis M. O'Leary, Aird & Berlis LLP
Counsel to EGD

_____
David Stevens, Aird & Berlis LLP
Counsel to EGD

EB-2007-0731

**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 the balance and clearance of the Class Action Suit Deferral Account;

**AND IN THE MATTER OF** an application by Enbridge Gas Distribution Inc. for an order or orders amending or varying the rates charged to customers for the sale, distribution, transmission and storage of gas commencing January 1, 2008.

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# BOOK OF AUTHORITIES OF ENBRIDGE GAS DISTRIBUTION INC.
# January 25, 2008

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EB-2007-0731

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