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February 14, 2012

BY EMAIL & COURIER

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St, Suite 2701
Toronto ON M4P 1E4

Dear Ms. Walli:

Board File No. EB-2011-0277
Enbridge Gas Distribution Inc. – 2012 Rates Adjustment
Energy Probe – Submissions

Pursuant to Directions provided by the Board Panel during the Oral Hearing on January 25, 2012, please find the Argument of Energy Probe Research Foundation (Energy Probe) in the EB-2011-0277 proceeding for the consideration of the Board.

Should you require additional information, please do not hesitate to contact me.

Yours truly,

David S. MacIntosh
Case Manager

cc: Norm Ryckman, Enbridge Gas Distribution Inc. (By email)
Fred D. Cass, Aird & Berlis LLP (By email)
Randy Aiken, Aiken & Associates (By email)
Intervenors of Record (By email)

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Ontario Energy Board

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, 2012.

**ENERGY PROBE RESEARCH FOUNDATION
("ENERGY PROBE")**

ARGUMENT

February 14, 2012

**ENBRIDGE GAS DISTRIBUTION INC.
2012 RATES**

EB-2011-0277

ARGUMENT OF ENERGY PROBE RESEARCH FOUNDATION

A - INTRODUCTION

This is the Argument of the Energy Probe Research Foundation ("Energy Probe") on the unsettled issues in the matter of an application by Enbridge Gas Distribution Inc. ("EGD") for approval of rates set for 2012 under the multi-year Incentive Rate Mechanism ("IRM") as approved by the Board under File No. EB-2007-0615.

A Settlement Agreement in this matter was filed with the Board on November 29, 2011 and accepted by the Board in its Partial Decision and Order dated December 1, 2011. The Board held an oral hearing on the remaining unsettled issues on January 24 and 25, 2012. EGD filed their Argument in Chief on February 3, 2012.

The following submissions of Energy Probe deal with the issues that were not settled.

B. ISSUE 9 - IS THE AMOUNT PROPOSED FOR THE Y FACTOR - GAS COST & CARRYING COST APPROPRIATE?

Energy Probe has had the opportunity to review the submissions of the Canadian Manufacturers & Exporters ("CME") with respect to this issue. Energy Probe supports the submissions of the CME.

C. ISSUE 10 - IS THE NATURE OF, AND THE AMOUNT PROPOSED FOR, THE Z FACTOR - 2012 PENSION FUNDING REQUIREMENT APPROPRIATE?

Energy Probe submits that the 2012 pension funding requirement does not qualify for Z factor treatment in that it violates two of the criteria that have to be met, as set out in the EB-2007-0615 Revised Settlement Agreement. EGD has provided these criteria at paragraph 24 of its Argument In Chief dated February 3, 2012.

In particular, Energy Probe submits that the costs associated with the 2012 pension funding requirement fail to meet the criteria that states the cost must be beyond the control of Enbridge's management and is not a risk in respect of which a prudent utility would take risk mitigation steps and the criteria that states that the cost increase/decrease must not otherwise be reflected in the per customer revenue cap.

Management Control

Energy Probes submits that the pension related cost increase is clearly within the control of EGD's management. To begin with, EGD management agreed to a change in the requirement for employee contributions to fund the pension plan. Prior to 2001, employee contributions were required, however under the current agreement, no employee contributions are required or permitted (Exhibit B, Tab 2, Schedule 5, Appendix B, page 27). Obviously this change was agreed to by management and was not out of their control.

Further, as Ms. Trozzi stated (Tr. Vol. 1, page 175), EGD could ask for employee contributions to help fund the plan. She went on to indicate that it is not a road that they have gone down at all, because it would change their total compensation package. She further explained that EGD would want to look at the total compensation package, not just the pension piece. If EGD were to ask for contributions, then they would allocate that money that would be put into the pension plan elsewhere within the total compensation package. She concluded that the cost of the company would still be the same. She confirmed that EGD has the right in their relationship with the pension plan members to request up to the \$16.6 million in order to fund the carrying costs of that obligation.

Mr. Monteiro indicated that EGD could ask for contributions from the members but that would require an amendment to the terms of the plan (Tr. Vol. 1, pages 176-177). Ms. Trozzi indicated that would entail negotiations with the union through the collective bargaining process and that EGD has decided not to do that (Tr. Vol. 1, page 177).

Energy Probe submits that this description of what EGD could have done and what it has decided to do and not to do clearly indicates that these costs, and the recovery of these costs is clearly within management control.

EGD submits that if it required pension plan members to fund all or some of the \$16.6 million that it seeks to recover from ratepayers, it would have to increase compensation to its employees elsewhere within the total compensation package. Energy Probe submits that this is an implicit agreement by EGD that the \$16.6 million is part of its total employee compensation package. It is ludicrous for EGD to claim that its total employee compensation package is outside of management control.

In the EB-2011-0054 Decision and Order dated December 28, 2011 (and as corrected on December 30, 2011), the Board states that (page 13):

"Compensation is an area of specific concern to the Board. The Board notes Hydro Ottawa's compensation costs are based largely on negotiated settlements with its unionized workforce. The Board further notes that that the management compensation increases are tracking upward at the same pace as those settled on in negotiated settlements. These increased costs have been incurred at a time when compensation related benefit costs of various types have also increased. The Board recognizes that these particular benefit costs may not be under complete management control but the same cannot be said for the cost increases incurred in direct salaries to the management group nor the costs that are a result of the negotiations with the unionized employee group. It is the Board's expectation that costs be contained as a whole and where there is little the company can do to control costs in some areas it must make up for it in areas where it does have control." (emphasis added)

Energy Probe submits that the pension costs are part of the overall total compensation package, as described by EGD, and that management has control over this package. The company may not be able to control the need for the \$16.6 million related to pensions, but it does have control over who pays for its (employees or ratepayers), while at the same time controlling costs in other areas of the total compensation package. By trying to identify this cost as a Z factor, management is trying to get out of managing the issue and passing the costs onto ratepayers. Energy Probe submits that the Board should find that this is inappropriate in an IRM environment where the company has over earned on a gross revenue sufficiency basis in each year from 2008 through 2011 by an aggregate amount of \$112.6 million (Exhibit J2.4).

Finally Energy Probe notes that EGD has not provided any evidence in this proceeding related to the overall employee compensation costs, of which the pension cost is but one component. This is because, Energy Probe submits, EGD knows that employee compensation is within the control of management and clearly would not qualify as a Z factor event.

Cost Increase Not Reflected in Per Customer Revenue Cap

EGD claims that the cost increase related to the pension cost is not reflected in the per customer revenue cap. Energy Probe strongly disagrees.

Mr. Monteiro explained that the reason that the pension plan is in deficit now compared to a surplus a year ago is mainly that interest rates have declined very significantly (Tr. Vol. 1, pages 111-112). He further agreed that the deficit was primarily caused by the decline in interest rates that reduced the discount factor which gives rise to the deficit (Tr. Vol. 1, page 166, lines 1-6). Mr. Kancharla also agreed that the primary component of the Z factor claim was the decline in interest rates (Tr. Vol. 1, page 166, lines 19-21).

Mr. Thompson, on behalf of the CME, compared the impact on the cost of debt with the cost of the pension plan costs in that both reflect changes in interest rates (Tr. Vol. 1, page 167-168). On behalf of EGD, Mr. Culbert explained that it was EGD's view that there is no requirement for a Z factor for those elements of cost of capital and that there was to be no change in costs of capital for rate-setting purposes. Mr. Culbert suggested that all cost of capital were considered when determining what was to change in rates under the IRM term and suggested that a Z factor change for ROE or other elements of the cost of capital would be contrary to the rate-setting mechanism (Tr. Vol. 1, pages 168-169). Energy Probe notes that a review of the EB-2007-0615 Settlement Agreement indicates that the return on equity would not be subject to adjustment under the IRM term. There is no mention of any cost of debt adjustment, one way or the other.

As shown in Exhibit J1.9, Attachment 1, the cost of debt (short term and long term) forecast for 2012 is \$144.7 million, a reduction of \$21.7 million from the \$166.4 million included in the 2007 Board Approved revenue requirement. Energy Probe submits that if it is appropriate to include an increase of \$16.6 million related to pension costs that are driven by the decline in interest rates, then it is also appropriate to include the reduction of \$21.7 million in debt costs associated with the same decline in interest rates.

The question, then, is whether or not either of these adjustments related to the decrease in interest rates qualify as a Z factor. Energy Probe submits that the answer is no.

Changes in interest rates are captured in the per customer revenue cap through the application of the GDP IPI FDD inflation measure. This macroeconomic measure of inflation captures changes in prices in all components of the economy including (but not limited to) labour, materials, energy and capital.

Interest rates are simply the price of capital and is no different than a change in labour costs, energy costs or material costs. All of these changes in costs are captured in the macroeconomic inflation factor. As a result the GDP IPI FDD index already captures and reflects the change in the price of capital. Including a change in costs driven by a change in interest rates in a Z factor would result in a double counting of the impact and should be denied by the Board.

Finally, Energy Probe notes that the increase in total compensation costs would be treated in the same manner as described by Mr. Culbert with respect to the reduction in the cost of debt (Tr. Vol. 1, page 168). To the extent that there is a cost or benefit that flows through to the bottom line, that will be taken care of in the earnings-sharing mechanism that is part of the overall IRM package.

D. ISSUE 11 - IS THE NATURE OF, AND THE AMOUNT PROPOSED FOR, THE Z FACTOR - 2012 CROSS BORES/SEWER LATERALS APPROPRIATE?

Energy Probe has had the opportunity to review the submissions of the CME with respect to the cross bore safety program. Energy Probe supports those submissions.

Causation

The first criteria for an event to qualify as a Z factor, is that the event must be causally related to an increase/decrease in cost (see paragraph 24 of the Argument In Chief). Ms. Lawler agreed that the projected spending on cross bores is not because of the TSSA order (Tr. Vol. 2, page 128, lines 20-28). In fact, EGD made it clear that it is going to spend the forecasted amount on the issue regardless of whether there was a TSSA order. EGD further agreed that there was no component of its spending on cross bores that is specifically caused by the TSSA order; the only thing the TSSA order required was that EGD do a plan. This plan did not involve the spending of any incremental money (Tr. Vol. 2, page 129, lines 1-13).

Energy Probe submits that the TSSA order cannot be the event that caused an increase in costs. EGD states that the costs would be incurred whether or not there was such an order and that there was no increase in costs related to the TSSA order. As a result, the TSSA order does not qualify as Z factor event as it fails to meet the first of the five criteria to be considered as a Z factor.

Management Control

The second criteria for Z factor eligibility listed by EGD in paragraph 24 of their Argument In Chief, is that the cost must be beyond the control of management and is not a risk in respect of which a prudent utility would take risk mitigation steps. Energy Probe submits that the cross bore issue fails to meet this eligibility criteria.

The cross bore issue is clearly not outside of EGD's management control because they were aware of the issue as far back as 2004 related to an incident with St. Lawrence Gas (Tr. Vol. 2, page 96, lines 19-28). St. Lawrence Gas is a fully owned subsidiary (Tr. Vol. 2, page 127-128).

Ms. Lawler indicated that EGD became aware of the risk in 2004 but did not feel that it was an applicable risk to their franchise area. Clearly this was a management decision. Ms. Lawler agreed that this decision was the management response to the risk that had been identified (Tr. Vol. 2, page 97, lines 1-5).

The cross bore program is part of an existing program at EGD falling under pipeline integrity and safety wherein EGD seeks to try and ensure that people do not damage the natural gas facilities and cause release of gas (Tr. Vol. 2, page 95). This pipeline integrity program has an associated budget of \$20,487,840 in OM&A and an additional \$20,091,118 for capital in 2012. The forecasted revenue requirement associated with cross bores of approximately \$3.8 million (Exhibit B, Tab 2, Schedule 6, page 16, paragraph 32), which represents a small fraction of the overall budget. The OM&A cost of \$3.7 million represents 18% of the budget and the capital expenditures of \$2.1 million represent just over 10% of the budget.

Energy Probe submits that the costs associated with the cross bore issue are more properly described as part of the ongoing costs associated with pipeline integrity and safety. These costs are not beyond the control of management, as the issue was known to EGD well before the 2007 cost of service application that set rates that formed the basis for IRM rates for the following five years. It was management's decision that this was not a risk for their franchise area. They were wrong. EGD is now trying to recover costs that it says are incremental because they chose not to include anything in base rates.

Energy Probe submits that it is not appropriate for EGD to claim a Z factor event based on a management decision that turned out to be wrong. The cost forecast by EGD is a direct result of decisions made under management control and therefore do not meet the eligibility criteria for a Z factor.

E. ISSUE 13 - IS IT APPROPRIATE TO ESTABLISH FOR 2012 THE PROPOSED PENSION FUNDING COST VARIANCE ACCOUNT ("PFCVA")?

If the Board determines that the 2012 pension funding requirement qualifies as a Z factor (see Issue 10 above), then Energy Probe submits that it is appropriate to establish the Pension Funding Cost Variance Account ("PFCVA") for 2012 as requested by EGD.

The final cost associated with the pension funding in 2012 is not known at this time and is subject to several variables that will determine the final figure. The use of the PFCVA will ensure that both EGD and its ratepayers are protected in that the costs recovered from ratepayers will be equal to the costs actually incurred by EGD.

F. ISSUE 14 - IS IT APPROPRIATE TO ESTABLISH FOR 2012 THE PROPOSED CROSS BORES COST VARIANCE ACCOUNT ("CBCVA")?

If the Board determines that the 2012 costs associated with the cross bores/sewer laterals qualifies as a Z factor (see Issue 11 above), then Energy Probe submits that it is appropriate to establish the Cross Bores Cost Variance Account ("CBCVA") for 2012 as requested by EGD.

Again, this will protect ratepayers and EGD in that ratepayers will only pay for the actual costs incurred by EGD and EGD will recover its actual costs.

Energy Probe notes that EGD agrees that if the 2012 revenue requirement turns out to be less than \$1.5 million, then the amounts collected in rates would be refunded to ratepayers (Argument In Chief, page 21). Energy Probe submits that this would be appropriate since the Z factor event would not meet the materiality threshold.

G. ISSUE 15 - IS IT APPROPRIATE TO ESTABLISH FOR 2012 THE PROPOSED TRANSITION IMPACT OF ACCOUNTING CHANGES DEFERRAL ACCOUNT ("TIACDA")?

Energy Probe does not oppose the creation of the proposed transition impact of account changes deferral account. However, Energy Probes notes that this account is needed essentially as a record to track differences between CGAAP and USGAAP in 2012 and that whether or not the account is approved by the Board, EGD will be applying in the 2013 rate case to recover amounts associated with change in accounting rules (Tr. Vol. 2, page 73-74). EGD also confirmed that it is not necessary to have a deferral account to track differences and that this tracking can be done outside of the regulatory accounting sphere (Tr. Vol. 2, page 74, lines 14-19). EGD also confirmed that this account is not needed for any 2012 rate-making purpose; nor is it needed to reflect any uncontrollable costs being incurred in 2012 (Tr. Vol. 1, page 74, lines 20-24).

In light of the preceding, Energy Probe submits that the Board should consider whether it should approve a deferral account for which the applicant has admitted it does not require for regulatory purposes.

If the Board does accept the creation of this account for 2012, Energy Probe submits that the Board should make it clear that the amount to be recorded in and/or cleared from the account, including the amortization period associated with any such clearance will be dealt with in a future proceeding.

H. ISSUE 17 - IS THE PROPOSED COST ALLOCATION OF THE TWO NEW Z FACTORS APPROPRIATE?

EGD proposes to allocation the pension funding requirement proportionately to the allocation of the 2012 distribution revenue requirement (excluding the proposed Z factors) (Exhibit B, Tab 3, Schedule 1, page 8). The allocation of costs associated with the cross bores is proposed to be allocated on the basis of the service allocation.

EGD provided further analysis and rationale for choosing each of the proposed cost allocation methodologies in the response to part (c) of Exhibit I, Tab 5, Schedule 5. As noted in the responses to parts (d) and (e) of that same Energy Probe interrogatory, EGD states that the allocations it is proposing in this proceeding closely approximate the allocation that would have been used had these costs been included in the 2007 cost of service application.

Energy Probe, therefore, submits that the Board should approve the allocations as proposed by EGD if both or either of the Z factor requests are approved by the Board.

I - COSTS

Energy Probe requests that it be awarded 100% of its reasonably incurred costs for participating in this proceeding. Energy Probe has co-operated with other intervenors to ensure no duplication of effort.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

February 14, 2012

Randy Aiken

Consultant to Energy Probe