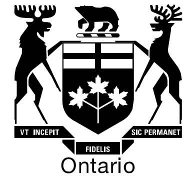
**Ontario Energy Board** **Commission de l'énergie de l'Ontario**




**EB-2011-0277**

**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.

**BEFORE:** Paul Sommerville
Presiding Member

Ken Quesnelle
Member

**DECISION AND ORDER**
**May 10, 2012**

Enbridge Gas Distribution Inc. ("Enbridge" or the "Company" or the "Applicant") filed an application on September 1, 2011 (the "Application") with the Ontario Energy Board (the "Board") under section 36 of the *Ontario Energy Board Act, 1998*, S.O. c.15, Sched. B for an order of the Board approving or fixing rates for the sale, distribution, transmission and storage of natural gas, effective January 1, 2012. The Board assigned file number EB-2011-0277 to the Application.

The Application is for rates for 2012 to be set under the guidance of the multi-year Incentive Regulation plan methodology as approved by the Board under File No. EB-2007-0615 (the "IR Plan"). 2012 is the fifth and final year of the five-year plan. The rates under the plan are adjusted each year by the application of a Distribution Revenue Requirement per Customer Formula.

A Settlement Agreement was filed on November 29, 2011 that indicated a settlement had been reached among the parties on most of the issues in the proceeding, with the exception of the following seven issues for which there was no settlement:

- Y factor - Gas Cost & Carrying Cost (Issue 9)
- Z factor – 2012 Pension Funding (Issue 10)
- Z factor – 2012 Cross Bores / Sewer Laterals (Issue 11)
- Variance account for Z factor - 2012 Pension Funding (Issue 13)
- Variance account for Z factor - 2012 Cross Bores / Sewer Laterals (Issue 14)
- Transition Impact of Accounting Changes Deferral Account (Issue 15)
- Cost allocation of Z factors (Issue 17)

The Board accepted the Settlement Agreement on December 1, 2011 and issued an Interim Rate Order on December 9, 2011 which gave effect to the proposed rates on an interim basis beginning January 1, 2012. The Interim Rate Order excluded the revenue requirement impact of the two Z factors noted above.

The Board held an oral hearing on the unsettled issues on January 24 and 25, 2012.

At the conclusion of the oral hearing, the Board set out the schedule for parties to make submissions on the unsettled Issues. Enbridge filed its Argument-in-Chief on February 3, 2012. Submissions by intervenors and Board staff were filed on February 14, 2012, and Enbridge's reply was filed on February 24, 2012.

The Board received submissions from Board staff, the Association of Power Producers of Ontario ("APPrO"), the Building Owners and Managers Association Toronto ("BOMA"), the Consumers Council of Canada ("CCC"), Canadian Manufacturers & Exporters ("CME"), Energy Probe Research Foundation ("Energy Probe"), the Federation of Rental-housing Providers of Ontario ("FRPO"), the Industrial Gas Users Association ("IGUA"), School Energy Coalition ("SEC") and the Vulnerable Energy Consumers Coalition ("VECC").

In this Decision and Order, the Board will make findings on each of the unsettled issues.

## Y factor - Gas Cost & Carrying Cost (Issue 9)

### Background

The Y factor for "gas cost & carrying cost" is the pass-through cost of the upstream gas supply portfolio including transportation and storage costs. It also includes the carrying cost of gas storage and working cash related costs associated with the gas portfolio. Several parties have taken issue with Enbridge's proposed Y factor gas costs for the 2012 rate year.

Each year, Enbridge develops a gas supply portfolio to meet the expected needs of its customers for the upcoming year. In developing this portfolio, Enbridge makes arrangements for the supply and transportation of gas to meet annual, seasonal and peaking needs. The elements of the gas supply portfolio include Western supplies, peaking contracts, Chicago supply, delivered supply, gas in storage, long haul transportation on the systems of TransCanada Pipelines ("TCPL"), Alliance and Vector, short haul contracts on the TCPL system, such as Storage Transportation Service (STS), and transportation on the Union Gas system to move gas from Dawn to Parkway in Ontario.

On September 30, 2011 the Company filed its 2012 gas supply plan as part of its pre-filed evidence package. The plan revealed that the Company modified its gas transportation plans for 2012 by acquiring an additional 75,000 GJ/day of TCPL STFT ("Short Term Firm Transportation") capacity for three winter months. This was done because Enbridge had concerns about the reliability of a portion of its gas deliveries. The concern was that the same gas suppliers have been providing Peaking Services, Direct Purchase Supplies and Curtailment Delivered Supplies. In January and February of 2011, certain direct purchase customers had their deliveries cut by their suppliers and one of Enbridge's peaking suppliers failed to deliver gas when called upon, as a result of that supplier having its supplies cut. Based on these events and the expected demands on the system in 2012, Enbridge took the step of, among other things, acquiring the additional 75,000 Gj/day of TCPL STFT. Enbridge said that this step was needed to meet expected demands in the winter of 2012.

The evidence indicates that the cost associated with Enbridge's decision in this respect may be upwards of $7.8 million in 2012.

In a Decision and Order dated August 26, 2010, the Board approved a System Reliability Settlement Agreement in proceeding EB-2010-0231. The System Reliability Settlement Agreement was the product of a lengthy consultation process that Enbridge undertook with its stakeholders. The terms of the System Reliability Settlement Agreement were designed to address Enbridge's concerns about the reliability of direct purchase gas deliveries showing up on its system on peak winter days.

CME, FRPO and IGUA took issue with the Company's decision to acquire the additional 75,000 GJ/day of STFT for the three winter months in 2012. These parties were concerned about the extra gas costs and, in addition, held the position that before implementing this new supply into its 2012 gas supply portfolio, Enbridge was obligated to consult with the parties to the System Reliability Settlement Agreement proceeding.

The parties focussed on the provisions of the System Reliability Settlement Agreement around the 200,000 GJ/day of STFT service that, according to the agreement, Enbridge was permitted to acquire from TCPL as part of the agreement. In respect of this 200,000 GJ/day of STFT, the System Reliability Settlement Agreement states as follows:

> Enbridge will reduce the amount of peaking supplies held under contract as part of its gas supply portfolio by 200,000 GJ/day and it will replace these peaking supplies with an equivalent volume (200,000 GJ/day) of TCPL STFT service from Empress that it will secure annually, or, if economic, equivalent firm transportation. The 200,000 GJ/day of STFT service contracted for annually by Enbridge will be for a period of three months (not limited to calendar months) over the winter throughout the term of the Long Term Resolution, unless otherwise agreed to by the parties or ordered by the Board. The STFT service will be utilized in lieu of an equivalent amount of peaking supplies in peak and near-peak conditions. In addition, STFT service was to be used to displace other winter purchases, when it is economic and operationally appropriate to do so.[1]

The parties argued that in light of this provision of the Settlement Agreement, and another provision in respect of reporting to the parties on material changes in circumstances, Enbridge is required to consult with the parties about any gas supply plan that involves more than 200,000 GJ/day of STFT. Parties said that the additional amount of 75,000 GJ/day for 2012 was material in the context of the System Reliability Settlement Agreement.

[1] System Reliability Settlement Agreement EB-2010-0231 pages 9 and 10 of 16.

CME submitted that not only was there an obligation on Enbridge to consult with the parties, but that the System Reliability Settlement Agreement was breached and the Board should therefore disallow a portion of Enbridge's costs for its 2012 gas supply portfolio. CME suggested an amount representing the incremental cost of the 75,000 GJ/day of STFT, which was estimated to be about $7.8 million, be disallowed. CME was the only party to submit that the Board should disallow a portion of the Y factor for gas costs.

Board staff and FRPO suggested that Enbridge should conduct stakeholder consultations during its annual gas supply planning exercise and that such consultations would be beneficial to all parties for a number of reasons. The benefits cited by Board staff included the promotion and improvement of stakeholder understanding of the gas supply planning exercise.

Enbridge objected to holding such stakeholder consultation meetings on the basis that they would be neither practical nor reasonable.

In reply, Enbridge provided its interpretation of the section of the System Reliability Settlement Agreement pertaining to the 200,000 GJ/day of STFT. Enbridge's contention is that the agreement obliges it to hold to the timing and duration of the contracted service, unless otherwise agreed to by the parties or ordered by the Board to do otherwise. It submitted that the agreement does not limit it to the quantum of 200,000 GJ/day. Enbridge submitted that the section of the agreement relied on by CME and others does not include language regarding consultation.

### Board Findings

The Board has carefully considered the evidence of the Company and the submissions put forward by the parties. The Board finds that there has not been a breach of the System Reliability Settlement Agreement in respect of the additional volumes contracted for the winter of 2012. The Board accepts Enbridge's interpretation of the agreement and agrees that no consultation was required in its consideration to contract for the additional service. The Board will not direct that there be a cost disallowance and will not direct that any action be taken. The Board hereby approves the 2012 gas cost Y factor for recovery by Enbridge.

## Z factor – 2012 Pension Funding (Issue 10)

### Background

Enbridge's Application included a request for a Z factor in the amount of $16.6 million to fund a deficit in its pension plan. Enbridge's evidence indicated that the deficit arose as a result of changes to Ontario pension regulations; notably, changes introduced to the *Pension Benefits Act* of Ontario on June 23, 2009. Enbridge's evidence is that actuarial valuations of the pension plan are typically carried out every three years, and Enbridge's most recent valuation was done as of December 31, 2009. At that time, it showed the Company's pension plan to be in a surplus position.

The new regulations require pension plan sponsors who are currently enjoying a contribution holiday to file an annual cost certificate with the Financial Services Commission of Ontario ("FSCO") to prove that their plans remain in a surplus position. If the cost certificate shows that the pension plan is not in a surplus in any year, then contributions must be made to cover the annual services cost of the plan. Enbridge's evidence is that it has been on such a contribution holiday and accordingly, had to prepare the required cost certificate. Enbridge indicates that last October, it prepared an estimate of its pension plan position at year end 2011. Enbridge's evidence is that the estimate showed that its pension plan had shifted to a deficit position in 2011, mostly due to financial market conditions, and most particularly due to low interest rates. A contribution requirement was therefore triggered and the required funding translated to a contribution equal to the annual services cost in 2012. Enbridge estimated this at $16.6 million for 2012, the amount of the requested pension funding Z factor. Enbridge indicated that the final cost certificate was expected to be available by late February or March in 2012. The witnesses testified that they did not expect the annual services cost to be materially different than what appeared in the estimate of $16.6 million. Enbridge requested a variance account around the Z factor to true-up to the actual amount expended on pension funding in 2012.

Enbridge submitted that the payment of pension costs for employees is a legitimate and prudent cost to support the provision of service to Enbridge's customers. Enbridge said that its funding request meets all of the Z factor criteria.

The Z factor criteria are set out in the Settlement Agreement in Board proceeding EB-2007-0615 [2].

(i) the event must be causally related to an increase/decrease in cost;
(ii) 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;
(iii) the cost increase/decrease must not otherwise be reflected in the per customer revenue cap;
(iv) any cost increase must be prudently incurred; and
(v) the cost increase/decrease must meet the materiality threshold of $1.5 million annually per Z factor event.

Intervening parties APPrO, BOMA, CCC, CME, Energy Probe, SEC and VECC were opposed to the Z factor. The submissions of these parties were that the subject pension costs are within the control of management and that the underlying event that triggered the Z factor expense is low interest rates. This is in contrast to what Enbridge cited as being the triggering event, that being the legislative requirements of the government under the *Pension Benefits Act.* The intervenors submitted that changes in interest rates do not qualify for Z factor treatment. The parties further argued that if the Board decides in favour of granting the Z factor, then on fairness grounds, there should also be a credit to ratepayers for Enbridge’s reductions in debt related expenses during the IR Plan term, also due to low interest rates.

Board staff took the view that the pension funding matter should be a shared cost responsibility to be shared equally between ratepayers and shareholders.

Enbridge replied that the parties were trying to recharacterize the Z factor as something other that what it is and in so doing, have attempted to disqualify it from the Z factor criteria. Enbridge also objected to the parties attempting to treat anything that relates to management activities as being within the control of management and hence not eligible for Z factor recovery. Enbridge maintained that the pension cost Z factor request lies outside of the control of management.

## Board Findings

The position of the Company is that it is entitled to Z factor treatment for mandated increases to pension funding. In 2009, after the IR Plan was in place, the provincial

[2] EB-2007-0615 Decision of the Board, Sched. A, p. 21 (EB-2007-0615, Ex. N1-1-1, p. 21).

government made some changes to the regulatory environment respecting pension funding. The change that is relevant for this proceeding required a report, including a certificate from pension administrators respecting the "solvency" of their respective plans, and created an obligation on the part of pension administrators to increase contributions to address any apparent shortfalls.

The pension fund that is the subject of the Applicant's request is a noncontributing pension plan. That is to say that the employees, the beneficiaries of the plan, are not obliged to make any contribution to the plan.

As a result of this regulatory change the Applicant was required to file a report which showed that after a period of a contribution holiday on the part of the Applicant, a nominal shortfall had arisen which would require contribution by the Applicant in 2012 of $16.6 million. It is this payment which the Applicant has requested be included in rates for 2012 as a Z factor. Issue 13 addresses the creation of a variance account to capture over or under contributions during the period.

It is common ground that the definition of Z factor which is relevant to the Board's consideration of this request appears in the Settlement Agreement presented by the parties at the commencement of the IR Plan period. In order to qualify for Z factor treatment, the cost must meet the Z factor criteria. If it fails to meet one of the criterion, it fails to qualify as a Z factor.

It is the Board's view that the Applicant's request fails on two of the five criteria established for qualification as Z factor. It fails on the first criterion which is the cause of the event and it fails on the second criterion which relates to the cost being beyond the control of management. There is no serious question in this case as to whether the costs meet the materiality threshold, which for Enbridge is $1.5 million.

The event which was causally related to the nominal shortfall in the pension plan is the relatively poor performance of the financial markets, and is perhaps most particularly, the fall in interest rates which have characterized financial markets for the last several years. This underperformance has reduced the returns the Company was relying upon to maintain the buoyancy of its pension fund. We use the word nominal to describe the shortfall because there is no actual funding crisis associated with the underperformance of the plan. The Company is an ongoing operation with very significant assets, revenues and opportunities and there is no evidence of any actual difficulty in meeting the

obligations the Company assumed when it created the plan. The provincial regulator in making the changes that it did in 2009 imposed the reporting and contribution requirement to avoid such a crisis in the future.

The Board finds that the cost of this Z factor is within the control of management and represents a risk in respect of which a prudent utility would take risk mitigation steps. The Board's analysis of this question begins with the assumption of those obligations by the Company at the time that the plan was created. There is no obligation under the law to offer employees noncontributory pension benefits. The Company voluntarily assumed the obligations that it did under the plan with a view to attracting and maintaining a workforce that it felt it needed to fulfill its business goals. In accepting that range of responsibilities voluntarily, the Company also accepted the contingencies and vicissitudes that attend that choice in not requiring contributions from employees. It accepted the risk that it would be solely responsible for the funding of the plan. The funding of the plan was and is dependent upon sound investment choices and the overall performance of the financial markets. In the Board's view, the adoption by the Company of a noncontributory pension plan carries with it the risk that the funding of the plan might require extraordinary contributions from time to time, depending on the performance of the financial markets and interest rates. While the Company may not bear responsibility for, and may have no ability to influence interest rates or the overall performance of the financial markets, it does have the ability, and did exercise its judgment in making investment decisions which did not yield results sufficient to fund the plan. That is not to say that the Board would require the Company to meet an unrealistic standard of success in its investment decisions, especially at a time when the markets were generally underperforming. But when it adopted the noncontributory pension plan, it accepted the responsibility to maintain funding for it.

In addition, the risk of underperformance is a risk that the Company ought to have anticipated and taken steps to address. If one thing is predictable about financial markets it is that there is an element of volatility to them, and that markets can materially underperform according to projection. In the Board's view this is a risk for which the utility ought to have made provision. It is a risk that a prudent utility should take steps to mitigate.

The Board also does not consider the introduction of the reporting/certification requirement to be a genuine exogenous triggering event for the Z factor. It is true that the reporting requirement led to the requirement to resume funding of the pension plan,

but the genuine cause for the requirement to resume funding was the underfunding of the plan for the years prior to the report. The regulatory intervention by government in this case did no more than oblige the plan administrator to resume funding where there was an apparent shortfall - it did not create a novel or additional obligation to fund the plan. That obligation was adopted by the Company when it accepted the plan in the first place. The regulatory intervention which is relied upon by the Company as the triggering event merely brought to the Company's attention the need to meet its obligations under the plan.

For these reasons the Board denies the Company's request for Z factor treatment for the pension funding requirement.

**Z factor – 2012 Cross Bores / Sewer Laterals (Issue 11)**

**Background**

Enbridge requested a Z factor in the amount of $3.8 million in 2012 to cover the cost of reducing the potential of dangerous events occurring associated with any cross bore situations that exist on its service lines.

According to Enbridge's evidence, the cross bore scenario occurs as a result of an undetected penetration of a sewer line by a natural gas service line during trenchless installation of the gas line. A cross bore will present a safety issue if a person attempts to clear a blocked sewer line and in so doing ruptures the intersecting gas line. In this scenario, gas could seep into the building through the sewer line and create a potential for explosion due to the gas being ignited (by a pilot-light for example).

The Technical Standards and Safety Authority of Ontario ("TSSA") issued a directive on August 31, 2011 to gas distributors in the province which required the preparation of an action plan to deal with cross bore issues. The action plan for addressing cross bores was required to be submitted to the TSSA by October 30, 2011. Enbridge's action plan was included in the pre-filed evidence. It carried an estimated total cost of $5.8 million but only $3.8 million was proposed in the Z factor for 2012 recovery. This amount represented the revenue requirement impact of addressing cross bore issues in 2012. Enbridge requested a variance account around the Z factor to true-up to the actual amount expended on cross bore related work in 2012.

Enbridge's evidence is that it first became aware of the cross bore issue in 2004 when it gained knowledge of an incident that occurred in the United States and that its first recorded cross bore incident occurred in Innisfil, Ontario in May 2007.

Enbridge submitted that the cross bore request meets each of the qualifying Z factor criteria. The Z factor criteria are set out in the IR Plan Settlement Agreement in Board proceeding EB-2007-0615 [3].

(i) the event must be causally related to an increase/decrease in cost;
(ii) the cost must be beyond the control of Enbridge's management and is nota risk in respect of which a prudent utility would take risk mitigation steps;
(iii) the cost increase/decrease must not otherwise be reflected in the per customer revenue cap;
(iv) any cost increase must be prudently incurred; and
(v) the cost increase/decrease must meet the materiality threshold of $1.5 million annually per Z factor event.

Intervening parties BOMA, CCC, CME, Energy Probe, FRPO, IGUA, SEC and VECC were opposed to the Cross Bore Z factor. The reasons given by these parties were that the Z factor event was not triggered by the TSSA directive as Enbridge had argued, but rather it was a known risk in existence for some time and was controllable. The parties submitted that given the nature and history of the expenditures on the cross bores, Enbridge has demonstrated that it is currently managing these costs under its pipeline integrity and safety program and therefore these are costs that are clearly within the control of management.

The parties argued that no extra funding is required because Enbridge should be able to manage this type of ordinary operational costs within the overall cost allowance envelope provide by the IR Plan.

Board staff submitted that the Z factor should be approved because cross bores are a safety issue that requires funding per the TSSA directive. Board staff submitted that the utility's actions leading up to the formal TSSA requirement were prudent and that it could not avoid the cost.

[3] EB-2007-0615 Decision of the Board, Sched. A, p. 21 (EB-2007-0615, Ex. N1-1-1, p. 21).

Enbridge replied that the costs at issue were not included in the utility's base IR Plan rates and are therefore incremental costs. Enbridge also said that the arguments that it should be able to absorb the costs are without merit as this was never part of the Z factor test criteria. Enbridge reiterated that it has met all of the IR Plan Z factor criteria and that the arguments of the parties mischaracterize its submissions on the issue.

**Board Findings**

The evidence indicated that over the last number of years there has been a ripening concern over this potential, which culminated in a TSSA directive, dated August 31, 2011, which required the Applicant and other gas distributors to prepare an action plan to deal with cross bore issues. The Applicant filed its action plan on October 30, 2011 and the costs associated with it for 2012 amount to $3.8 million.

The requirement of the TSSA to file the action plan is considered by Enbridge to be the triggering event for the Z factor claim.

Once again, consideration of this request is made pursuant to the criteria for Z factor eligibility set out in the Settlement Agreement approved at the commencement of the IR Plan. As noted above there are five factors, as provided for in the Settlement Agreement which are required to be met in order for a particular cost to qualify for Z factor treatment. These are set out in the background discussion above. In order to qualify for Z factor treatment the claim must meet each of these requirements. If it fails one test, then it fails to be eligible for Z factor treatment.

With respect to this claim, some parties asserted that the claim did not meet the materiality threshold of $1.5 million. While the amount claimed is $3.8 million, which clearly exceeds the $1.5 million threshold, they argue that not all of that sum is genuinely attributable to the specific requirements of the action plan within 2012. For the reasons stated below, the Board does not need to decide whether the claim meets the materiality threshold.

The Board finds that the request for Z factor treatment of the cross bores fails with respect to two of the tests associated with the Z factor definition in the Settlement Agreement. These two tests are those that relate to management's control of the costs and the triggering event that gave rise to the Z factor claim.

First, the Board does not consider the management and control of issues related to cross bores to be matters that are in any meaningful sense beyond the control of management. The provision of gas to its customers in a safe and reliable manner is the fundamental undertaking of the utility. There are many challenges associated with accomplishing that goal, and at its core the utility is organized, staffed and financed in order to be able to meet that standard. The innovation of trenchless pipe placement introduced inherent risks due to the inability to physically see the end to end placement of the gas service pipe as it is placed in its operating position. As a new procedure, the Board expects that Enbridge would have taken steps to identify and mitigate any new risks associated with its implementation. This type of risk analysis and mitigation is essentially no different than the risk management associated with the installation and maintenance of the distribution infrastructure as a whole within the franchise. As previously stated, that fundamental undertaking is precisely what the management of Enbridge is engaged in organizing and executing. The fact that a previously unidentified risk has now been identified does not take the responsibility to identify this type of risk out of the realm of the basic undertaking of the utility.

Further, the risk of interference with distribution infrastructure is precisely the kind of risk that a prudent utility would be fully engaged in managing and mitigating. There is nothing on the record to suggest that that is not exactly what Enbridge has been doing since the cross bore possibility started to emerge as an industry issue a number of years ago. It is the Board's finding that this is precisely what a prudent utility would do, and, in this case, has done.

The TSSA regulatory innovation in this case, which the Company describes as the triggering event, is nothing more than a codification of what a prudent utility would have, should have, and has been doing as its awareness of the cross bore evolved over the last number of years. It is telling, and comforting, that the utility has been directly involved with the regulator, in this case the TSSA, to develop the action plan requirement that gives rise to this claim. However, the TSSA codification of the response to cross bores is not the causal event underlying the Z factor claim.

For these reasons the Board denies the Company's request for Z factor treatment related to cross bore management.

**Variance account for Z factor - 2012 Pension Funding (Issue 13)**
**Variance account for Z factor - 2012 Cross Bores / Sewer Laterals (Issue 14)**
**Cost allocation of Z factors (Issue 17)**

In view of the fact that the Board is not approving either of the Z factors, there is accordingly no need to make a determination on whether the variance accounts are needed, or a determination on any cost allocations related to the Z factors.

## Transition Impact of Accounting Changes Deferral Account (Issue 15)

### Background

Enbridge has requested that the Board establish a 2012 Transition Impact of Accounting Changes Deferral Account ("2012 TIACDA") in order to recognize and record the financial impacts that will occur in relation to its transition to a new accounting standard. Enbridge has transitioned from Canadian Generally Accepted Accounting Principles ("CGAAP") to United Sates Generally Accepted Accounting Principles ("USGAAP") as of January 1, 2012 for financial accounting purposes. Enbridge stated that the purpose of establishing the 2012 account is to reflect financial impacts that will occur in 2012.

As mandated by the Canadian Accounting Standards Board, Enbridge was required to move away from CGAAP beginning January 1, 2012. The Company has identified a significant impact related to Other Post Employment Benefits ("OPEBs") which are post-employment benefits other than pension plans, such as dental plans, medical plans and life insurance coverage.

Unlike pensions, however, there is no standalone trust or plan that holds the funds for future payment of OPEBs. Enbridge therefore carries a balance sheet liability with respect to payments to be made to retired employees or future retired employees. Until the end of 2008, Enbridge accounted for OPEBs on a cash basis but as of 2009, CGAAP required that Enbridge convert from the cash basis to the accrual method. At the time of conversion, Enbridge recorded a regulatory offset on its balance sheet which essentially made the recording of OPEBs equivalent to the cash method. With Enbridge's transition away from CGAAP, the Company must adjust its balance sheet

OPEBs liability to an accrual basis and remove the OPEBs regulatory offset account through a charge to retained earnings.

Enbridge has proposed to record all accounting differences between CGAAP and USGAAP in the 2012 TIACDA. However, the only difference that has been identified to date is related to the treatment of OPEBs.

Enbridge proposed that the amount to be charged to the 2012 TIACDA be represented as follows:

1) The difference between the cash amount to be paid out by Enbridge and the OPEBs expense calculated in accordance with the accrual basis of accounting for each of the 2011 and 2012 fiscal years. This amount is estimated to be approximately $3 million for each of the two years; and

2) The charge to Retained Earnings in Enbridge's 2010 USGAAP financial statements resulting from the removal of the regulatory offset account and the setting of the OPEBs liability in accordance with USGAAP. This amount is estimated to be approximately $84 million.

Enbridge indicated that the total amount proposed to be recorded in the 2012 TIACDA related to OPEBs is therefore $90 million as at the end of 2012 which represents the cumulative difference between the accrual method versus the cash method. Enbridge currently recovers OPEBs from its ratepayers using the cash method. The $90 million would be a ratepayer charge.

Parties making submissions on this issue included Board staff, BOMA, CCC, CME, Energy Probe, and SEC. Most of the parties took the position that the 2012 TIACDA should not be established at this time. Many said that there is no legitimate regulatory purpose for the account and that it should be summarily rejected on that basis. CCC and Energy Probe stated that if there is a legitimate regulatory purpose, then they would not oppose its establishment, but submitted the onus is on the Enbridge to justify why the account needs to be established.

CME and SEC argued that there is a retroactive rate making element or "out of period" request for rate relief inherent in the 2012 TIACDA request. Parties argued that Enbridge undertook accounting actions related to the OPEBs unfunded liabilities in

2009, 2010 and 2011 without prior Board approval and that these actions have culminated in the current request for the 2012 TIACDA. They argued that the Board normally rejects such requests because they represent an "out of period" adjustment or retroactive rate making.

CME submitted that in determining the questions around the OPEBs accounting, the Board would need to step back in time and consider the issues that Enbridge would have faced had it applied in a timely manner in its 2009 rate case to establish a regulatory asset account relating to its unfunded OPEBs liability.

CME submitted that the issue should be deferred to and fully scrutinized in the 2013 rate rebasing application already filed with the Board under file number EB-2011-0354. Several parties submitted that if the Board does approve the account, it should be made very clear that any disposition would be dealt with in a future proceeding.

Board staff submitted that Enbridge's argument for establishing the 2012 TIACDA is not compelling because the Board does not regulate the utility's internal accounting processes or its external financial reporting. Board staff noted that it is up to the individual utility to decide how it wants to track the amounts that arise due to a transition of accounting standards. This extends to satisfying any financial reporting requirements outside of the regulatory arena. Board staff submitted that this account is solely related to the utility's external financial reporting regime and has nothing to do with regulatory costs recognized by the regulator for ratemaking purposes. Board staff also stated that the timing of this application is out of sequence in that there exists no Board approval to use USGAAP for rate regulation purposes. This determination is expected to take place in the 2013 cost of service rate rebasing proceeding. Until that happens, Board staff submitted the deferral account request should be held in abeyance.

In addition, Board staff pointed out that there is heightened complexity in the current rate application. This is because the amount proposed for the 2012 TIACDA represents the cumulative difference between the cash basis of accounting for OPEBs expense that Enbridge has been recovering from ratepayers, and the accrual basis that Enbridge will be proposing to switch to for ratemaking purposes in 2013. The complexity arises because this cumulative difference has a multi-year history that would require closer examination in a future rate proceeding.

Enbridge rejected all arguments about retroactive ratemaking because the transition to USGAAP is being made in 2012 and therefore the account is proper and relevant to the year of transition. Enbridge submitted that are a number of reasons that support approval of the 2012 TIACDA and that no party has identified any prejudice that will be caused if the account is approved with the express stipulation that approval does not presume or imply any outcome with respect to disposition.

**Board Findings**

The Board will approve the establishment of the 2012 TIACDA. The Board's view is that the account is needed to appropriately track the effects of the change in accounting standard to USGAAP as at January 1, 2012.

The Board finds that the establishment of the deferral account is consistent with the guidance provided in the EB-2008-0408 Addendum to the Report of the Board regarding the implementation of International Financial Reporting Standards ("IFRS") dated June 13, 2011.

The Board notes that effective January 1, 2012 Enbridge must transition away from CGAAP to another accounting standard (either IFRS or USGAAP). In order to ensure that balances arising from this transition have eligibility for recovery in rates, should any such eligibility be so determined in the future, it is appropriate to approve the establishment of the deferral account at this time.

The Board's view is that the establishment of the 2012 TIACDA is not contingent on whether the Board approves the use of USGAAP for rate regulation purposes in the 2013 rates proceeding. There is no valid reason that the Board should defer its decision on this matter until the Board has considered and issued its decision regarding the use of USGAAP by Enbridge for rate regulation purposes. If approval to use USGAAP for ratemaking purposes is not forthcoming, the 2012 TIACDA would no longer be required, as the balances recorded in the account would simply not be recognized for rate regulation purposes.

For absolute clarity, the Board stresses that by approving the set-up of the 2012 TIACDA, the Board is in no way presuming or implying that amounts in the deferral account will be approved for disposition. Similarly it does not in any way imply that the Board will approve Enbridge's request to move to USGAAP for regulatory accounting

purposes in the 2013 cost of service rebasing case. There will be a Board process for disposition determination. This is consistent with the principles applied by the Board in previous deferral account matters.

The Board notes Board staff's comments with respect to the complexity associated with the OPEBs differential. On this point, the Board expects Enbridge to thoroughly explain how the OPEBs impacts came about in the 2013 rebasing proceeding where it is expected to be heard.

As noted in the Addendum to the Report of the Board, the Board does not prescribe financial reporting for regulated utilities, nor does the Board govern the principles of financial reporting. The Board does, however, set the requirements for regulatory accounting and it is from this perspective that the Board finds it appropriate to establish the requested deferral account. The Board acknowledges that alternative tracking methodologies exist for financial reporting purposes; however, for rate regulation purposes, the regulatory deferral account mechanic is the accepted and established regulatory accounting practice of the Board.

The Board recognizes that while the only costs that have been identified in the 2012 TIACDA are those related to the cash basis versus the accrual basis for the OPEBs liability, Enbridge may be still studying the matter for additional impacts. While more precision would be preferable, it is simply not available now, and the Board's view is that the analysis may be more conclusive at a later date. Rather than restricting the account to OPEBs impacts only, the Board will approve a more open-ended account. Additionally, given that the accounting standard financial impacts relating to OPEBs represent a non-cash transaction, the Board finds that no interest shall be applicable to the account.

## Implementation

The 2012 rates in effect now are interim rates, per the Board's December 9, 2011 Interim Rate Order. The revenue requirement underpinning the interim rates reflects the requested 2012 revenue, less the amounts proposed for the Z factors. The interim rates were implemented and made effective on January 1, 2012.

The Board notes that as a result of this Decision and Order, there is no impact on the 2012 revenue requirement already approved on an interim basis. This is because the Board has rejected both the Z factor requests. The Board will therefore declare the interim rates “final” in this Decision and Order. Accordingly, there is no need for the Company to prepare a draft final rate order.

## Cost Awards

The Board may grant cost awards to eligible stakeholders pursuant to its power under section 30 of the *Ontario Energy Board Act, 1998*. When determining the amount of the cost awards, the Board will apply the principles set out in section 5 of the Board’s *Practice Direction on Cost Awards*. The maximum hourly rates set out in the Board’s Cost Awards Tariff will also be applied.

The Board will issue a Decision on Cost Awards after the steps set out below have been completed.

## THE BOARD ORDERS THAT:

1. The interim rates approved by the Board in its Interim Rate Order 2012 IRM Adjustment dated December 9, 2011 shall be final rates.

2. Enbridge shall establish a 2012 Transition Impact of Accounting Changes Deferral Account (“2012 TIACDA”). The balances in the account shall not attract interest charges.

3. A decision regarding cost awards will be issued at a later date. Parties eligible for a cost award shall submit their cost claims within 14 days from the date of this Decision. A copy of the cost claim must be filed with the Board and a copy is to be served on Enbridge. Cost claims must be prepared in accordance with the Board's Practice Direction on Cost Awards.

4. Enbridge will have until 21 days from the date of this Decision to object to any aspect of the cost claims. A copy of the objection must be filed with the Board and one copy must be served on the party against whose claim the objection is being made.

5. Any party whose cost claim was objected to will have until 28 days from the date of this Decision to make a reply submission as to why their cost claim should be allowed. One copy of the submission must be filed with the Board and one copy is to be served on Enbridge.

All filings to the Board must quote file number EB-2011-0277 and consist of two paper copies and one electronic copy in searchable / unrestricted PDF format filed through the Board's web portal at www.errr.ontarioenergyboard.ca. Filings must clearly state the sender's name, postal address and telephone number and, if available, a fax number and e-mail address. Please use the document naming conventions and document submission standards outlined in the RESS Document Guideline found on the "e-Filing Services" webpage of the Board's website at www.ontarioenergyboard.ca. If the web portal is not available you may email your document to BoardSec@ontarioenergyboard.ca.

**DATED** at Toronto, May 10, 2012

**ONTARIO ENERGY BOARD**

*Original Signed By*

Kirsten Walli
Board Secretary