EB-2012-0055

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 clearance or disposition of amounts recorded in certain deferral or variance accounts.

REPLY ARGUMENT OF ENBRIDGE GAS DISTRIBUTION INC.

Introduction

1. On May 11, 2012, Enbridge Gas Distribution Inc. (Enbridge) filed an application with the Board for an order or orders approving the disposition of balances in certain deferral and variance accounts. On September 17, 2012, the Board approved the Settlement Agreement that resulted from the Settlement Conference in this proceeding.[1] As a result of the approval of the Settlement Agreement, two issues remained for hearing in this case.[2]

2. One of the two outstanding issues relates to the 2011 Earnings Sharing Mechanism Deferral Account (2011 ESMDA) and concerns "the amount of the provision for uncollectibles for the purposes of the 2011 earnings sharing calculation".

3. The second outstanding issue relates to the 2011 Transactional Services Deferral Account (2011 TSDA) and is specifically laid out in the Settlement Agreement in the following manner:

> Has Enbridge treated the upstream transportation optimization revenues appropriately in 2011 in the context of Enbridge's existing IRM agreement?

4. The hearing of these two issues proceeded on November 22, 2012 and, following the conclusion of the oral phase of the hearing, the Board issued a procedural order setting a schedule for written submissions.[3] Pursuant to the provisions of this

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[1] Decision and Order on Settlement Agreement, September 17, 2012.
[2] In accordance with the provisions of the Settlement Agreement, a third issue was addressed in the context of Enbridge's 2013 rate case (EB-2011-0354).
[3] Procedural Order No. 2, November 29, 2012.

procedural order, Enbridge received a Staff Submission from Board staff and it received written argument from five intervenors, as follows: Canadian Manufacturers & Exporters (CME), Consumers Council of Canada (CCC), Energy Probe Research Foundation (Energy Probe), Federation of Rental-housing Providers of Ontario (FRPO) and Vulnerable Energy Consumers Coalition (VECC)

5. This is the Reply argument of Enbridge submitted in accordance with the Board's procedural order. Enbridge will respond to the arguments of others with respect to the two outstanding issues under the headings that follow.

Provision for Uncollectible Amounts

6. According to the Board's Notice of Application & Procedural Order No. 1 issued on June 4, 2012, there are more than 15 intervenors in this case. Out of this large group of intervenors, VECC is the only participant in this proceeding which has argued that the outcome of the issue regarding the provision for uncollectible amounts (allowance for doubtful accounts) should be an increase in the amount shared with ratepayers through the 2011 ESMDA.

7. It is worthy of note that VECC did not in any way participate in the oral hearing of the two outstanding issues in this case that proceeded on November 22, 2012. In particular, VECC did not take the opportunity afforded by the oral hearing to put questions to Enbridge's witness panel regarding the provision for uncollectible amounts. This is particularly important, Enbridge submits, given the contents of VECC's argument.

8. VECC's argument refers to "three additional issues" in relation to the provision for uncollectible amounts.[4] VECC's argument also relies on an assertion that a particular aspect of the evidence "is not clear to VECC".[5] VECC could have participated in the oral hearing in order to ask the witness panel about the "three additional issues" and to seek clarity about the area of uncertainty referred to in VECC's argument.

9. Enbridge submits that the Board should give little or no weight to VECC's final argument, given that it is based on perceived issues never put to the witnesses by VECC and VECC's own uncertainty about an aspect of the evidence that VECC never sought to clarify with the witnesses.

10. The provision for uncollectible amounts was addressed, or at least touched upon, in the arguments of two other parties, Energy Probe and CCC, and in the Staff

[4] Final Submissions on Behalf of the Vulnerable Energy Consumers Coalition (VECC argument), page 9.
[5] VECC argument, page 8.

Submission. The Staff Submission concluded that no adjustment is required to the 2011 ESMDA[6] and CCC stated that it "adopts the submissions of Board Staff".[7] Energy Probe also supported the position of Enbridge; it reached the conclusion that the "adjustments applied in 2011 have no net adverse impact on ratepayers".[8]

11. The Staff Submission captures the essence of the evidence with respect to the provision for uncollectible amounts, as is reflected in the following submissions made by Board staff:

> ...Enbridge's estimate of the allowance for doubtful accounts was made using the best information available at the time. Furthermore, Enbridge's adjustment to the allowance for doubtful accounts is the result of new information provided by the implementation of the CIS rather than correction of an accounting error.[9]

12. In contrast, Enbridge submits that VECC's argument is rife with misconceptions of the evidence and the applicable accounting standards, including the following:

> (a) VECC says that it is not clear why Enbridge should not "attempt to collect these specific amounts from the specific customers".[10] In fact, the evidence is clear that Enbridge attempts to collect all of its accounts receivable over an average period of 27 months.[11] (Emphasis added.)
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> (b) VECC refers to "assigning ... $4.1 million as a Provision for Uncollectible Accounts".[12] In fact, the amount of $4.1 million referred to by VECC was a reduction to the provision for uncollectible amounts in 2010 that resulted in higher earnings sharing than would have otherwise been the case in 2010.[13]
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> (c) VECC questions why Enbridge discovered reporting deficiencies in 2012.[14] In fact, the evidence is that the reporting deficiencies came to

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[6] Staff Submission, page 6.
[7] Written Argument of the Consumers Council of Canada (CCC argument), para. 3.
[8] Energy Probe argument, page 9.
[9] Staff Submission, page 6.
[10] VECC argument, page 8.
[11] Ex. K1.2, Question 3.
[12] VECC argument, page 9.
[13] Ex. K1.2, Question 7.
[14] VECC argument, page 9.

light in 2011.[15]

(d) VECC expresses its belief that there has been "an accounting error requiring a true-up".[16] In fact, there is no evidence in this case of any accounting error; as recognized in the Staff Submission, the estimate of the provision for uncollectible amounts is made on the best available information at the time of the estimate and an adjustment resulting from the availability of new information is not "an accounting error".[17]

(e) VECC suggests an issue with respect to "intergenerational inequity",[18] but the provision for uncollectible amounts does not flow through to rates determined on the basis of Enbridge's Incentive Regulation (IR) formula; this case simply involves an earnings calculation that is based on the best available information about the provision for uncollectible amounts at a particular point in time.

13. Section 1506 of the Canadian Institute of Chartered Accountants (CICA) standards notes that many items in financial statements can only be estimated and, in this regard, it refers specifically to bad debts.[19] Section 1506 goes on to say that "[t]he use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability".[20] Section 1506 also explicitly recognizes that an estimate may need revision in different situations, including "new information".[21]

14. In accordance with the CICA standards, Enbridge's provision for uncollectible amounts is an estimate that is based on the best information available to management at the time of making the estimate. The provision is adjusted each month on a prospective basis when new or better information becomes available.[22] An increase in the provision for uncollectible amounts serves to reduce income in the month when the change is booked;[23] this is required by section 1506 of the CICA standards, which says that the effect of such a change in an accounting estimate shall be recognized prospectively in net income.[24]

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[15] Ex. K1.2, Question 7.
[16] VECC argument, page 8.
[17] Ex. K1.4, General Accounting Section 1506, paragraph .34.
[18] VECC argument, page 9.
[19] Ex. K1.4, General Accounting Section 1506, paragraph .32. See also Ex. K1.2, Question 2.
[20] Ex. K1.4, General Accounting Section 1506, paragraph .33.
[21] Ex. K1.4, General Accounting Section 1506, paragraph .34.
[22] Ex. K1.2, Questions 1 to 5.
[23] Ex. K1.2, Question 4.
[24] Ex. K1.4, General Accounting Section 1506, paragraph .36.

15. As pointed out by Energy Probe, the Board-approved Settlement Agreement which established the terms and parameters of Enbridge's IR plan, contains the following provision regarding the Earnings Sharing Mechanism (ESM):

> ...for the purpose of the ESM, Enbridge shall calculate its earnings using the regulatory rules prescribed by the Board, from time to time, and shall not make any material changes in accounting practices that have the effect of reducing utility earnings ... .[25]

Also as pointed out by Energy Probe,[26] there has been no material change in accounting practices by Enbridge. The evidence is that Enbridge has used the same accounting treatment with respect to its Accounts Receivable and provision for uncollectible amounts in a consistent manner for at least the last twenty years; more specifically, there has been no change to Enbridge's accounting practices in these areas during the IR term.[27]

16. Enbridge therefore agrees with the submission of Board staff that no adjustment is needed to the 2011 ESMDA.[28]

Optimization

17. The submissions of intervenors regarding the treatment of upstream transportation optimization revenues reveal a variety of different approaches to this issue, although a recurring theme relates to the recent Board decisions with respect to transactions effected by Union Gas Limited (Union). Enbridge submits that there are important starting points for the Board's consideration of the arguments made by intervenors.

18. One important starting point is the issue as framed in the Board-approved Settlement Agreement for this case. As set out above, the issue is as follows:

> Has Enbridge treated the upstream transportation optimization revenues appropriately in 2011 in the context of Enbridge's existing IRM agreement?

19. The issue as framed in the Settlement Agreement does not put into play a

[25] EB-2007-0615 Settlement Agreement, page 27.
[26] Energy Probe argument, page 9.
[27] Ex. K1.2, Question 5.
[28] Staff Submission, page 6.

general review of Transactional Services carried out by Enbridge. On the contrary, the issue is a very specific one with respect to upstream transportation optimization that is about:

- ~ the treatment of "revenues";
- ~ "in 2011"; and
- ~ "in the context of Enbridge's existing IRM agreement".[29]

20. Another important starting point is established in VECC's argument. As stated by VECC:

> ...EGD has acted in accordance with the agreed historic treatment of ... transactions and has not sought to gain any undue profit ... ."[30]

21. Given that Enbridge has acted in accordance with the "agreed historic" treatment of transactions, it is extremely difficult to see why the treatment of net revenues produced from those transactions in 2011 should be changed from that which has been applied and accepted in previous years. This is all the more so in light of the specific issue in this proceeding, which is framed "in the context of Enbridge's existing IRM agreement". As a result of the existing IR agreement, Enbridge's rates are set over a multi-year term on the basis of agreed-upon, Board-approved parameters and Enbridge submits that overall outcomes within the context of this plan should not be disrupted by changes to the "agreed historic" treatment of revenue from Transactional Services.

22. The primary reason given for a change to the agreed historic treatment of revenues from upstream transportation optimization seems to be consistency[31] or compatibility[32] with decisions rendered by the Board in cases involving Union. CCC submits, for example, that there should be "regulatory consistency" in the analysis of the appropriate treatment of upstream transportation activities, as between Union and Enbridge.[33]

23. For the reasons given below, Enbridge submits that the Board should reject the arguments that have been made about consistency or compatibility with decisions in Union cases. In any event, though, Enbridge submits that, from the point of view of "regulatory consistency", it is more important that the Board be consistent in its regulation of Enbridge, especially when Enbridge's approach is in accord with the

[29] EB-2012-0055 Settlement Agreement, page 12.
[30] VECC argument, page 6.
[31] CCC argument, paragraph 7.
[32] CME argument, paragraph 35.
[33] CCC argument, paragraph 7.

"agreed historic" treatment, than that the Board be consistent as between Enbridge and Union, especially when the circumstances of Enbridge and Union are so fundamentally different.

24. As to the differences between the circumstances of Enbridge and Union, CCC's view of these differences is set out in the following passage in its argument:

> The CCC acknowledges that the scale of Union's use of its RAM credits, and its deliberate creation of unabsorbed demand charges, makes Union's activities in the upstream transportation market superficially different from those of EGD. However, while the deliberate distortion of its gas purchase arrangements was a factor in the Union Decision, the critical feature was that the transactions were, at their core, part of the gas supply plan.[34]

25. The difference referred to in the first sentence of this passage from CCC's argument is far more than a "superficial" distinction, as asserted by CCC. The "deliberate creation of unabsorbed demand charges" referred to by CCC is fundamentally and radically different from anything done by Enbridge.

26. Even with this dismissive view of what it considers to be a superficial difference between Union and Enbridge, however, CCC unequivocally says that the "critical feature" of Union's activities was that "the transactions were, at their core, part of the gas supply plan". This "critical feature" of the Union cases, simply put, has no application whatsoever in the case of Enbridge. Enbridge's upstream transportation optimization activities are not, and cannot reasonably be perceived to be, at the core of Enbridge's gas supply plan.

27. The evidence in this case is absolutely clear that Enbridge does not develop a gas supply plan with a view to achieving future optimization transactions. As stated by Mr. Small in oral testimony:

> And certainly we don't go through and develop our supply plan to say, Okay. We think we'll be able to do these kinds of deals. In fact, we don't know – I don't know next summer what we're going to be doing. I can imagine we will probably be doing some deals, but the size and level or type of transaction remains to be seen.[35]

28. Enbridge's gas supply plan is developed in order to meet the seasonal and peaking demands of customers. As part of that gas supply plan, Enbridge has entered

[34] CCC argument, paragraph 21.
[35] Tr., page 61.

into a number of transportation contracts with TransCanada PipeLines (TCPL), Alliance Pipelines and Vector Pipeline. As stated in the response to Undertaking J1.1:

> One particular contract with TCPL is for Firm Transportation Service ("FT") from the Empress Receipt point to the Eastern Delivery Area ("EDA"). This contract assists EGD in its ability to meet peak, winter, and seasonal demands. EGD operates this contract at 100% Load Factor. In the winter, the Company relies on this contract as well as other services, such as storage withdrawals to meet the demand in the EDA. In the summer, the Company continues to flow this contract at 100% Load Factor with any gas in excess of demand in the EDA being diverted to storage.[36]

29. Opportunities for Enbridge to carry out Transactional Services do not arise from the gas supply plan; they arise from the weather and other circumstances that occur as Enbridge proceeds to implement the gas supply plan during the year in respect of which it was made. This was explained by Mr. Small in the following testimony with respect to Storage Transportation Service (STS):

> ...we have those contracts in place that allow us to ensure that we will be able to meet our peak day demands, but also our winter seasonable [seasonal] demands.
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> ...
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> So what will happen is, our gas control group is going to be – they're ultimately responsible for ensuring that the demands of the utility customer are going to be met each and every day, and over, you know, the course of the winter period.
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> ...but there's going to be situations throughout the winter period where they don't need 100 percent of it. So these RAM credits are going to start to accumulate.
>
> Well, what our gas control group is going to do is, they're going to hold off releasing those credits to our transactional service group until later in the month
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> ...
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> If later in the month, when gas control is looking out seven days towards the end of the month, depending upon how demand is, if they don't anticipate the need to move IT, they will turn to our transactional service group and say: If you can do a deal with a counterparty and it's going to require to move IT transport, go ahead.

[36] Response to Undertaking J1.1, page 1.

> ...
> So it becomes their decision as to the amount of capacity they would be willing to let the transactional services group release, if you will.
>
> So there are a number of factors that are going to go into the volume or the quantity that's going to be released from our gas control perspective, ...[37]

30. In short, it is simply wrong to think that Transactional Services are a core part of Enbridge's gas supply plan. They are a function of circumstances that arise, and factors taken into account by Enbridge's Gas Control group, as a gas supply plan is implemented. The "critical feature" referred to by CCC in relation to the cases involving Union is absent in the case of Enbridge and hence there is no inconsistency as between Union and Enbridge to support the argument that the Board should change the "agreed historic" treatment for Enbridge.

31. Energy Probe's argument appears to confuse the role of Enbridge's Gas Control group, as discussed by Mr. Small, with gas supply planning. Mr. Small's testimony set out in paragraph 29, above, explained how, as the gas supply plan is implemented in any particular month, the Gas Control group will take into account a number of factors before deciding whether capacity can be released to the Transactional Services group. Based on this testimony, Energy Probe says, in relation to the functions of the Gas Control group, that this is "an ongoing, annual planning exercise".[38]

32. The gas planning exercise, however, occurs in advance of the period (year) in question as Mr. Small determines how best to meet the seasonal and peaking demands of customers and the contracts needed for this purpose are put in place. Mr. Small's testimony about the Gas Control group was not describing the development of the gas supply plan; it was describing the implementation of the plan by the Gas Control group. The implementation of the gas supply plan by the Gas Control group is entirely in line with the underlying premise of Transactional Services, which is that when, during the course of a particular year, circumstances are such that the assets put in place for the purpose of meeting the demands of utility customers do not need to be utilized fully for that purpose, the use of the assets can be optimized through Transactional Services.

33. In their arguments, intervenors make submissions about different treatment of particular categories of upstream transportation optimization transactions. Certain of these submissions squarely contradict one another. For example, VECC submits that

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[37] Tr., pages 8 to 13.
[38] Energy Probe argument, page 4.

transactions that it refers to as STS RAM[39] transactions should be "classified as Gas Cost-Related and the net revenue flowed through the PGVA".[40] FRPO's submission on this point is as follows:

> Secondly, and very importantly, we recognize Enbridge's use of the STS-RAM credits. ...after the ratepayers' needs are addressed, additional credits could be used to derive additional value prior to expiry at the end of the month. We understand that the credits in the TSDA go back to ratepayers in proportion to their interest in the asset. In our view, this is what a utility ought to do with the RAM program. To the extent that unutilized credits are released for the opportunity of creating margin for ratepayer and shareholder value, we believe Enbridge is acting as it ought to as a public utility.[41]

34. Quite apart from the contradictory positions advanced in intervenor submissions, Enbridge submits that the attempts by intervenors to argue for different treatment of different categories of transportation optimization transactions are not helpful to the Board and, indeed, are not consistent with the evidence in this case. Mr. Small explained repeatedly that the categories of transactions referred to by intervenors are all really just exchanges of gas. He said, for example that a "capacity release" transaction is "still an exchange deal".[42] He said, as well, that:

> ...all three ... types of transportation optimization deals, in my mind, are simply exchanges. And they're exchanges that are going to come about because a third party wants to enter into a transaction with us.[43]

35. In other words, "an exchange is an exchange is an exchange". Further, the fact that STS RAM credits may be an element of certain exchanges does not mean that the transactions are fundamentally any different from exchange deals that Enbridge has been doing as part of Transactional Services for many years. As Mr. Small observed, transportation optimization transactions come about because a counterparty will see an opportunity that arises in the context of the tolling methodologies that exist at any particular point in time.[44] This was the essential nature of exchange transactions before the introduction of STS RAM credits, it continues to be the essential nature of the transactions with STS RAM credits in place and it would continue to be the essential

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[39] RAM stands for "Risk Alleviation Mechanism" (not "Risk Amelioration Mechanism", as stated by VECC at page 5 of its argument).
[40] VECC argument, page 6.
[41] FRPO argument, pages 7-8.
[42] Tr., page 11.
[43] Tr., page 60.
[44] Tr., pages 60-61.

nature of the transactions if STS RAM credits were to be terminated. As stated by Mr. Small:

> ...just because we're able to do a deal and take advantage of the STS RAM, that's just a function of TCPL's tolling ... .
> ...
>
> These types of deals, ... RAM may go away in a year, two years from now. We don't know. It depends on what happens with TransCanada. But there may be other opportunities as part of TransCanada's tolling methodology that will arise.
>
> So struggling with the idea of traditional and not traditional. I have a little bit of a concern. It's still an exchange to me between two points.[45]

36. Unlike some other intervenors, CCC does not seem to differentiate among categories of upstream transportation optimization transactions. CCC says that Enbridge's upstream transportation optimization activities should properly be characterized as gas cost reductions and the reductions should be recorded in the Purchased Gas Variance Account (PGVA) with a 90 per cent allocation to ratepayers.[46]

37. Enbridge's Transactional Services have for many years consisted of transportation optimization activities and storage optimization activities. CCC's position apparently is that one of these two areas of activity should be eliminated entirely from Transactional Services. Enbridge submits that this is not a determination that the Board should make in this case where, in accordance with long-established practices, Enbridge has recorded the net revenue from storage optimization and transportation optimization activities in the 2011 TSDA and the ultimate issue before the Board concerns the clearance of amounts in deferral and variance accounts including the 2011 TSDA.

38. FRPO advances a number of arguments that encourage Enbridge to engage in different approaches to contracting for upstream transportation. Among other things, FRPO asserts: "By simply leaving the pipe to the Eastern Delivery Area empty and nominating Interruptible Transportation (IT) from Empress to Dawn, the gas could be transported for a lower cost".[47] In fact, Enbridge has responded to FRPO's idea about "leaving the pipe empty" and has explained that, if Enbridge had proceeded in the manner suggested by FRPO, it would have generated at most $0.24/Gj, while, by

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[45] Tr., page 61.
[46] CCC argument, paragraph 25.
[47] FRPO argument, page 4.

entering into a transaction with a counterparty that is able to take advantage of price spreads at a number of different receipt and delivery points, Enbridge generated revenue of $0.38/Gj, thereby providing greater benefit to ratepayers.[48]

39. Actually, Enbridge raised six different areas of concern in response to the idea put forward by FRPO.[49] Needless to say, the only evidence on the record in this proceeding with respect to any of the suggestions made by FRPO is the evidence of Enbridge. Although the only evidence on the record in this proceeding is that of Enbridge, FRPO's argument attempts to respond to Enbridge's concerns with new evidence, including evidence cited by reference to another proceeding.[50] Further, FRPO's response to Enbridge's evidence is very disrespectful, to say the least. FRPO says, for example, that "Enbridge's stated concern of becoming a marketer is naïve at best and misleading or unhelpful at worst".[51]

40. Enbridge submits that, obviously, the issues before the Board in this case fall to be determined on the basis of the evidence on the record in this case. Enbridge urges the Board to disregard the factual assertions in FRPO's argument that are not based on the evidence in this case, as well as FRPO's disrespectful and unnecessary commentary on the evidence that actually is on the record in this proceeding.

41. In any event, though, Enbridge submits that FRPO's suggestions about different approaches that Enbridge might take to contracting for upstream transportation are beyond the scope of the issue in this proceeding. As clearly stated in the Settlement Agreement, in Procedural Order No. 2 and in this Reply argument, above, the issue in this case is whether Enbridge has treated upstream transportation "revenues" appropriately in 2011 in the context of Enbridge's existing IRM agreement. The issue is not the implications of transactions that were never carried out by Enbridge; the issue is whether the revenues from the transactions that Enbridge did carry out have been treated appropriately (insofar as their recording in the 2011 TSDA is concerned).

42. FRPO's argument explicitly accepts that there is no evidence in this case of "incremental contracting in 2011 beyond the utilities' [sic] needs".[52] Given that Enbridge's gas supply contracting was in accordance with the needs of the utility, the actions taken by Enbridge to optimize upstream transportation arrangements as the gas supply plan was implemented are very much in line with the purpose of Transactional Services, namely, to optimize assets when circumstances are such that they do not

[48] Tr., pages 34-35 and Response to Undertaking J1.1.
[49] Response to Undertaking J1.1.
[50] The footnotes on page 6 of FRPO's argument (as well as on page 8) include references to the EB-2011-0210 proceeding.
[51] FRPO argument, page 6.
[52] FRPO argument, page 7.

need to be utilized fully for the purpose of meeting the demands of utility customers. For these reasons, Enbridge submits that the Board should not change the "agreed historic" treatment of revenues from upstream transportation optimization.

43. Enbridge's transactions to optimize upstream transportation arrangements are essentially the same as they have been for a number of years and Enbridge submits that the Board's treatment of the revenues from those transactions should remain the same. Enbridge concurs with Board staff that "no adjustment is required to the 2011 TSDA".[53]

Conclusion

44. Enbridge therefore requests that the Board accept the balances recorded in the 2011 ESMDA and the 2011 TSDA and approve Enbridge's proposed disposition of those balances.

All of which is respectfully submitted.

December 21, 2012

Fred D. Cass
Counsel for Enbridge Gas Distribution Inc.

[53] Staff Submission, page 5.