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BY EMAIL and RESS

September 11, 2013
Our File No. 20120459

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
M4P 1E4

Attn: Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: EB-2012-0459 –Enbridge Rates – Preliminary Issue

We are counsel for the School Energy Coalition. Pursuant to Procedural Order #1, these are SEC's reply submissions with respect to the possibility of hearing a preliminary issue. We have attempted to ensure that these submissions do not repeat our initial submissions, filed on July 20, 2013.

The Basic Concern

SEC raised the possibility of a preliminary issue for procedural reasons. Our fundamental concern is that Enbridge has chosen to reject the decoupling of rates and costs that is a key component of the Board's IRM approach in most cases, and instead to propose a multi-year cost of service methodology.

Staff, Enbridge and others have made the point that Enbridge is entitled to apply for anything they want, unless there is an express Board policy placing a limitation on that scope. Even then, they can probably still apply, but the Board may not do a full review of a non-compliant application.

All of this is true, and SEC does not disagree in any way. However, it remains the Board's prerogative to determine the rate-setting methodology, as set out in section 36(3) of the OEB Act, as follows:

> *"In approving or fixing just and reasonable rates, the Board may adopt any method or technique that it considers appropriate."*

Our concern is that implicit in this section is the Board's obligation to put its mind to whether the Enbridge proposal, or some other rate-setting methodology, is the most appropriate for Enbridge in 2014 and beyond.

What Enbridge is proposing is that the entire proceeding will unfold and be completed based on the

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Enbridge preferred methodology. The Board will listen to all the evidence on Enbridge's expected cost of service – more than $6 billion - for the period 2014-2018. Then, around January or February, when this is all done, the Board will make a determination whether five year cost of service for Enbridge is the best rate-setting methodology. If the Board decides against multi-year cost of service, then all of the time reviewing costs will largely have been wasted, and the Board will still not be in a position where it has an alternative method before it.

This appears to us to be a strategic decision on the part of Enbridge, and it does have some logic. Six months into an expensive process, there will clearly be an unwillingness on the part of many of the parties, and perhaps even the Board, to start from scratch, even if the evidence shows that multi-year cost of service is not optimal. BOMA, for example, has already noted in their submissions the issue of timing of this application, and the low likelihood that new rates will be in place in a timely manner [BOMA submissions, p.2]. What will BOMA's position be in February, if the Board is asked to make a determination that Enbridge has not justified a multi-year COS rate-setting method, based on the evidence heard? Will it be influenced by the delay factor?

Another way of putting this is: How do we stop Enbridge's choice of rate-setting methodology from becoming, de facto, the only available choice?

There are three other problems that could arise at the end of the hearing process.

First, Enbridge may argue, at the end of the hearing, that the Board is prohibited as a matter of law from deciding on any other basis but multi-year cost of service, because doing so would infringe the Fair Return Standard. That is, the Board would be free to find that Enbridge's forecast costs are too high, and reduce them, but rates would still have to be set to recover the costs the Board finds to be reasonable, i.e. multi-year cost of service. As this argument goes, having heard the costs of Enbridge, the Board must find as a fact whether and to what extent those costs are reasonable, and then – knowing what the reasonable costs are – must set rates allowing the recovery of those costs.

Second, Enbridge may argue, at the end of the hearing, that there is insufficient evidence on alternatives to the multi-year cost of service approach, as they relate to Enbridge, so the Board is prohibited as a matter of law from deciding in favour of, for example, a price cap, etc. As a result, the Board would be forced to either accept the multi-year cost of service approach, or simply deny the application and require Enbridge to start from scratch, in February.

Third, depending on the costs to be recovered by Enbridge under a decision by the Board in favour of multi-year cost of service, parties to the EB-2011-0354 Settlement Agreement may then be in a position to argue that the Settlement Agreement is invalid due to material misrepresentation, and that any order of the Board based on that Agreement is also no longer valid.

SEC's proposed solution to these concerns, the three above plus the overriding issue of momentum and timing, was a preliminary issue proceeding. That would, if the multi-year cost of service approach was accepted, lengthen the proceeding and increase its cost. On the other hand, if the Board determined that multi-year cost of service was not appropriate, having a preliminary issue would reduce the length of the proceeding and reduce its cost, because Enbridge would get to true IRM proposals earlier.

Despite our proposed solution, we have no appetite for further procedural steps. Therefore, if the Board can satisfy itself that the concerns expressed above can be dealt with without having this initial step, SEC is more than happy with that result.

Specific Points Raised by Others

We should provide brief response to a few of the specific comments in the initial submissions of others:

1. Enbridge and others have argued that their application is similar to the Custom IR option available to electricity distributors. In fact, Board Staff makes the surprising statement that Custom IR is "a stated future direction of regulation by the Board". Custom IR for electricity distributors is a special rule in the 4th Generation IRM regime, designed to deal with special cases within the broad diversity of electricity distributors. Its use remains unknown, because no such applications have been filed as of yet, but there is no doubt that its purpose is to recognize and adjust for LDC diversity. The same diversity issues do not arise in gas distribution, so the analogy to Custom IR is inapt. For example, both Union and Enbridge have major capital projects over the next five years. Union has a method of dealing with that in their Settlement Agreement with their stakeholders. Something like "Custom IR" does not appear to be required.

2. Enbridge argues that its plan qualifies as IRM because it is a revenue cap proposal, and because it has this Sustainable Efficiency Incentive Mechanism. These are both red herrings:

    a. This proposal is a revenue cap only in the sense that every application is inherently a revenue cap, because it sets a cap on revenues for a future test period. For example, any cost of service application is a "revenue cap" in that sense, as is this one. It is clearly not a revenue cap in the IRM sense, since that methodology involves setting revenue on a formula basis.

    b. SEIM sounds nice, but in fact it is a proposal that, during the next five years, Enbridge be rewarded annually for promising to be more productive in the future. They also propose that no-one can ever, in the future, look to see whether they actually were more productive, as they said they would be.

    The Board has in fact characterized the nature of IRM in numerous decisions and reports. The most recent is in the Board's September 6, 2013 Draft Report in EB-2010-0379 for the electricity distributors' 4th Generation IRM, where the Board said [page 3 of the Report] "IR decouples the price that the distributor charges from its cost." Enbridge has never at any time said that this application has that necessary decoupling, and they can't. What is proposed is that prices be set entirely on the basis of a cost forecast, and, as we have noted in our August 7th letter, Enbridge freely admits this time after time. Calling it "Customized IR" does not, by itself, make it an IRM proposal.

3. On page 4 of their September 4th submissions, Enbridge note that they have already proposed an issue dealing with the rate-setting methodology. It is instructive to note that their proposed issue deals only with whether their proposal deals with certain specific objectives. It does not propose the real issue, which is "What is the appropriate method for setting the rates for Enbridge for the period commencing January 1, 2014?" In fact, under their formulation this question would be out of scope.

Alternatives

SEC is concerned – as we have noted in our letter on Monday – with how the Board will get before it evidence on alternative rate-setting methodologies. While the Board will of course be aware of the Union Gas price cap methodology (with a restricted capital adder) recently filed with the Board in EB-2013-0202, the Board would still need evidence on its applicability to Enbridge. In addition, there may be other alternatives that would be suitable.

There appear to be three ways that the Board can get that evidence:

1. The Board Staff experts, Pacific Economics Group, could provide an analysis of the options, including the potential applicability of the Union Gas deal to Enbridge. This may be the optimum approach, but SEC does not know whether the scope of PEG's workplan would include this type of deliverable.

2. Intervenors could be expected by the Board to retain their own experts to review the Enbridge situation, and provide evidence on potential IRM options. This would be quite unusual. Intervenors are not normally expected to provide substantive evidence going to the root of the rate-setting approach, although obviously it could be done. Further, this would probably delay the process somewhat, as the intervenor experts, after being retained, would have to have extensive access to Enbridge information (some of which is, of course, in the Application), before doing their own analysis and writing an expert report setting out the alternatives and their consequences. This timing question must be understood in the context of the fact that, until this spring, Enbridge was publicly advising all stakeholders of its intention to file an application quite similar to that set out by Union Gas in EB-2013-0202. Thus, until quite recently no intervenor would have even considered the possibility that an expert on the fundamental rate-setting structure would be required. The shift to multi-year cost of service came as a surprise.

3. The Board could proceed without having any evidence on alternative methodologies, simply accepting or rejecting the Enbridge proposal. If the Board rejected that proposal, it would then be up to Enbridge to propose something else in a new application.

Any of these could work, but SEC wishes to request of the Board that, in the event that no preliminary issue phase is ordered, all parties be provided with the clearest possible guidance on the Board's expectations regarding alternative rate-setting methodologies. As proposed by Enbridge, this is already a substantial and very complex proceeding. If alternative methodologies need to be explored during this process, this will require careful planning on the part of all parties involved in that.

Conclusion

SEC has concerns about the unusual structure of this Application, and has proposed a procedural solution to deal with those concerns. Our primary issue is that our concerns be addressed, and SEC welcomes any approach the Board prefers that does so.

All of which is respectfully submitted.

Yours very truly,
JAY SHEPHERD P. C.

Jay Shepherd

cc: Wayne McNally, SEC (email)
Interested Parties