



# **ONTARIO ENERGY BOARD**

## **STAFF SUBMISSION**

**Union Gas Limited**

### **2012 EARNINGS SHARING & DISPOSITION OF BALANCES IN DEFERRAL & VARIANCE ACCOUNTS**

**EB-2013-0109**

**November 26, 2013**

## Introduction

Union Gas Limited (“Union”) filed an application dated May 9, 2013 with the Ontario Energy Board (the “Board”) under section 36 of the Ontario Energy Board Act, 1998, S.O. c.15, Schedule B, for an order of the Board amending or varying the rate or rates charged to customers as of October 1, 2013 in connection with the sharing of 2012 earnings under the incentive rate mechanism approved by the Board as well as final disposition of 2012 year-end deferral account and other balances (the “Application”).

On June 25, 2013, the Board issued Procedural Order No. 1 which included a process for written interrogatories, and established dates for a Settlement Conference as well as the filing of a Settlement Proposal.

The Settlement Conference was held on August 1, 2013. A letter was filed on August 7, 2013 on behalf of Union and the intervenors that participated in the Settlement Conference. The letter noted that a formal settlement was not reached.

Union and the Parties agreed that there were no matters in dispute with respect to the balances to be cleared and the allocation to ratepayers for the following deferral accounts

- Short-Term Storage and Other Balancing Services (Account No. 179-70);
- Unbundled Services Unauthorized Storage Overrun (Account No. 179-103);
- Gas Distribution Access Rule Costs (Account No. 179-112);
- Late Payment Penalty Litigation (Account No. 179-113);
- Carbon Dioxide Offset Credits (Account No. 179-117);
- Average Use Per Customer (Account No. 179-118);
- International Financial Reporting Standards Conversion Costs (Account No. 179-120);
- Conservation Demand Management (Account No. 179-123);
- Harmonized Sales Tax (Account No. 179-124);
- Pension Charge on Transition to U.S. GAAP (Account No. 179-127); and
- Federal and Provincial Tax Changes.

On August 20, 2013, the Board issued Procedural Order No. 2 which established the dates for an Oral Hearing to hear the remaining issues. On October 22 – 24, 2013, the Board held the Oral Hearing to hear the following matters:

- Unabsorbed Demand Costs (Account No. 179-108);

- Upstream Transportation FT-RAM Optimization (Account No. 179-130) and associated impacts on the Earnings Sharing Calculation;
- Lost Revenue Adjustment Mechanism (Account No. 179-75);
- Demand Side Management Variance Account (Account No. 179-111);
- Shared Savings Mechanism Variance Account (Account No. 179-115);
- Demand Side Management Incentive Deferral Account (Account No. 179-126);
- Union's request for Deferral Clearing Variance Account (Account No. 179-132);
- Preparation of Audited Utility Financial Statements (Account No. 179-129);
- Exhibit A, Tab 3 (Allocation and Disposition of 2012 Deferral Account Balances; Federal and Provincial Tax Changes and 2012 Earnings Sharing Amounts);
- Exhibit A, Tab 4 (Incremental Transportation Contracting Analysis); and
- Exhibit B, Tab 5, Exhibit C, Tab 2 and Exhibit C, Tab 3 (Union's responses to the Board's EB-2011-0210 Gas Supply Plan Review and associated third party studies).

On the issue of the preparation of audited financial statements for the portion of Union's business that is subject to rate regulation, Union provided an addendum to its EB-2013-0109 evidence on July 26, 2013 (the "Addendum"). The Addendum, amongst other things, noted the following:

The attached evidence addendum provides an updated estimate of the cost required to prepare these financial statements and respond to the Board's directive. Union's estimate is \$1.3 million. The balance in the deferral account as of December 31, 2013 will be submitted for recovery from ratepayers as part of Union's 2013 deferral disposition proceeding.

The Board issued a Notice of Motion and Procedural Order No. 3 on October 25, 2013. The Board, on its own motion, determined that it would initiate a motion to review the Board's direction in its EB-2011-0210 Decision and Order requiring Union to annually prepare and file separate audited financial statements for that portion of its business that is subject to rate regulation. The Board noted that it would hear this motion within the EB-2013-0109 proceeding. The Board served the Notice of Motion on all intervenors of record in the EB-2011-0210 proceeding that were not intervenors in the EB-2013-0109 proceeding and gave them the opportunity to request intervenor status on the basis of the Motion. No requests for intervenor status were made in response to the Notice of Motion.

The following is Board staff's submission.

## **Gas Supply Plan**

### **Background and Evidence**

The Board, in its EB-2011-0210 Decision, approved Union's 2013 gas supply plan as filed. The Board noted, however, that it had concerns with Union's gas supply planning process, its planning methodology, and the resulting supply plan in light of Union's actions over the incentive regulation period. The Board directed Union to file with the Board, prior to its next rates proceeding, an expert and independent review of its gas supply plan, its gas supply planning process, and gas supply planning methodology.<sup>1</sup>

In response to the Board's directive, Union filed with the Board, as part of this proceeding, a report developed by Sussex Economic Advisors (the "Sussex Report"). Sussex noted that it reviewed the following gas supply planning activities:

- Guiding Principles;
- Design Day Demand Forecast;
- Implementation of the Plan; and
- Contracting/Transportation Path Decision Process.

Sussex noted that in addition to the above issues, it also reviewed Union's approach with respect to extracting value from gas supply assets (i.e. upstream transportation optimization).

The Sussex Report set out the following conclusions in regards to Union's gas supply plan:

- Union's primary gas supply planning principles of reliability and cost are reasonable, similar to other LDCs, and are reflected in the gas supply plan.
- Union's approach regarding design day demand forecasting (i.e., extreme cold weather conditions and a firm customer usage factor per degree day) is appropriate, similar to other LDCs, and reflected in the gas supply plan.
- The design day demand forecasting approach for Union North and Union South is consistent and aligned. Sussex noted that the Union North forecasted design day demand becomes a direct input into the gas supply design day plan, while the Union South forecasted design day demand is an input into the storage and transmission system plan; however, the process

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<sup>1</sup> EB-2011-0210 Decision and Order, p. 40.

used to develop the Union North and Union South design day demand forecast is similar.

- Union's gas supply portfolio for Union North and Union South reflect the circumstances of each area. The resultant gas supply portfolios for Union North and Union South are reasonable and appropriately sized.
- Union's approach to decontracting/recontracting is comprised of data gathering, quantitative and qualitative analysis, and documentation. This approach is consistent with the contract evaluation approach used by other LDCs, is similar to the Union Incremental Transportation Contracting Analysis, and is reasonable.
- While there are various alternatives used by LDCs to extract value from gas supply portfolio assets, the current approach utilized by Union leverages the core competencies of the Gas Supply and Storage & Transmission groups, is consistent with other approaches used by LDCs (e.g. asset management arrangements), and is reasonable.<sup>2</sup>

The Sussex Report also set out a number of recommendations. Some key recommendations set out in the Sussex Report are as follows:

- In general, Union should increase the level of documentation across departments with respect to the demand forecasting and gas supply planning processes.
- For Union South, the coldest observed temperature should be used to develop the design day weather standard. This would result in Union North and Union South having a consistent and similar approach regarding design day weather standards. If this recommendation is adopted for Union South, the design day weather standard would be 43.1 degree days rather than the current value of 44 degree days.<sup>3</sup>

Union stated in its evidence that it accepted all of Sussex's recommendations and is in the process of implementing those recommendations.<sup>4</sup>

Union, in its Argument-in-Chief, submitted that it responded appropriately to the Board's gas supply planning directive set out in its EB-2011-0210 Decision and Order. Union also submitted that, as reflected in the Sussex Report and the evidence at the hearing, Union's gas supply planning process, methodology and plan reflect

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<sup>2</sup> Exhibit C, Tab 2, pp. 1-3.

<sup>3</sup> Ibid at pp. 3-5.

<sup>4</sup> Exhibit B, Tab 5, pp.6-7.

appropriate planning principles that are applied objectively and produce a gas supply plan that is right-sized.<sup>5</sup>

### **Board Staff Submission**

Board staff is of the view that Union adequately responded to the Board's direction, as set out in its EB-2011-0210 Decision and Order, to review its gas supply planning process, its planning methodology, and the resulting supply plan.

Board staff has reviewed Union's evidence, including the Sussex Report, which was filed in response to the Board's directive. Board staff has no issues with Union's gas supply planning process, its planning methodology or the resulting gas supply plan.

### **FT-RAM related Upstream Transportation Optimization**

#### **Background and Evidence**

Union proposed that revenues generated from FT-RAM related upstream transportation optimization be classified and treated as utility earnings (subject to sharing through the ESM). Under Union's proposal, the FT-RAM optimization deferral account would have no balance and the amount to be shared with ratepayers would be \$15.73M. Overall, Union's proposal results in a \$0.2M debit being collected from ratepayers (this is comprised of a \$15.93M debit balance in the deferral accounts that are disposed of in the ESM proceeding and a \$15.73M credit related to earnings sharing).

Union stated that the evidence set out in its application supports its proposed treatment of the FT-RAM related revenues. Union noted that the Board, in this proceeding, has the benefit of comprehensive pre-filed evidence (which was not available in the 2011 ESM proceeding). Union noted that its evidence sets out, in detail, the context and nature of Union's upstream transportation optimization activities. Union argues that this evidence supports its position that the FT-RAM related revenues are appropriately treated as utility earnings subject to earnings sharing under the terms of the IRM Framework.<sup>6</sup>

In its evidence, Union set out the following reasons for treating the 2012 FT-RAM optimization revenues as utility earnings:

1. A key premise of the Board's EB-2012-0087 Decision with respect to the treatment of net FT-RAM revenue is that Union's gas supply plan was driven, in part, by optimization opportunities. Union noted that it provided evidence to

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<sup>5</sup> Union Argument-in-Chief, pp. 18 and 21.

<sup>6</sup> Union Argument-in-Chief, p. 4.

highlight that its gas supply plan is right-sized and does not consider opportunities for optimization.

2. The upstream transportation assets underpinning Union's gas supply plan are contracted based on a set of gas supply principles that are consistent with those used in other jurisdictions in Canada and the United States. Union stated that its gas supply plan does not have excess upstream capacity that can be used to facilitate transportation exchange services.
3. Notwithstanding the Board's EB-2012-0087 Decision, treating net FT-RAM revenue as a gas cost offset (Y-Factor) is inconsistent with (1) the historical treatment of upstream transportation exchange revenue; (2) the terms of Union's gas supply deferral accounts which were disposed of in 2012 by final orders of the Board in QRAM proceedings and which orders cannot be changed retroactively, and (3) represents a significant departure from the EB 2007-0606 and EB-2009-0101 Settlement Agreements for Union's IRM Framework for 2008-2012 approved by the Board.
4. The Board's EB-2012-0055 Decision (Enbridge Gas Distribution's 2011 ESM Proceeding) finding that temporarily surplus upstream assets may be used to support transportation exchange is consistent with how Union generates transportation exchange revenue.
5. Base exchanges and FT-RAM exchanges are transportation services sold to customers pursuant to a Board Approved rate schedule. Union stated that the noted transactions are fundamentally the same in that they use upstream transportation assets that are temporarily surplus, only differing as a result of the value provided by TCPL's FT-RAM service.
6. Union's proposed treatment of net FT-RAM revenue will ensure that a robust and active secondary market for transportation services will continue to exist and provide ongoing benefits to Ontario.<sup>7</sup>

Board staff has focused its submissions on whether Union's FT-RAM related optimization transactions occur on a planned basis (i.e. whether the gas supply plan is driven by optimization opportunities) and whether Union's FT-RAM related optimization transactions rely on assets that are temporarily surplus to the needs of Union's customers. As such, Board staff's summary of Union's evidence on the FT-RAM issue is limited to those areas.

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<sup>7</sup> Exhibit B, Tab 1, pp. 5-6.

Union noted that it applied the following criteria to determine if an FT-RAM transaction should be regarded as Transactional Service revenue subject to earnings sharing:

1. Temporarily Surplus - The exchange activity was served by some quantity of the upstream transportation capacity, and/or a portion of its path distance that was not required on a temporary basis to meet market area demands. Temporarily surplus capacity varies depending on weather and market demands.
2. Unplanned - The activity was unplanned in the sense that it was not included in the gas supply plan.
3. Sold as service - The exchange activity was a service provided to third parties. Union is not permitted to bundle the sale of gas and transportation, meaning that the only way to extract value is through transportation exchange transactions involving temporary surplus capacity to third parties.<sup>8</sup>

Union argued that all upstream transportation assets in the gas supply plan serve the purpose of meeting design day market demands and annual customer requirements. Union stated that any surplus that is available to support transportation exchange service activity (whether daily, monthly or seasonal) is only available on a temporary basis. The temporary surplus arises as a result of factors outside of Union's control, such as weather and consumption levels. Union stated that the surplus is not available on a planned basis.<sup>9</sup>

Union provided the following table which applies the criteria set out above to Union's transportation optimization activities.<sup>10</sup>

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<sup>8</sup> Union Argument-in-Chief, pp. 12-13.

<sup>9</sup> Ibid.

<sup>10</sup> Exhibit B, Tab 2, p. 9.



## 2 Evaluation of 2012 Transportation Exchange service and FT-RAM related activity

		2012 Results	Criteria			Conclusion*
			Temporary Surplus	Unplanned	Sold as Service	
<b>Utility Use of FT-RAM</b>						
①	System Supply Balancing (LBA)	\$0.6 M	✓	✓	X	Cost Reduction
②	System Supply Balancing (UDC Assignments)	\$6.7M	✓	both planned and unplanned	N/A	Cost Reduction
Total Utility Benefit						\$7.3M
<b>Transportation Exchange Services</b>						
③	Transportation Exchanges - Base	\$14.3M	✓	✓	✓	Revenue
Total Transportation Exchanges - Base						\$14.3M
<b>Transportation Exchange Services and Use of FT-RAM</b>						
④	Transportation Exchanges - FT-RAM related (Summer**)	\$3.7M	✓	✓	✓	Revenue
⑤	Transportation Exchanges - FT-RAM related (Winter)	\$1.8M	✓	✓	✓	Revenue
⑥	Transportation Exchanges - Transportation Assignments (Summer**)	\$25.9M	✓	✓	✓	Revenue
⑦	Transportation Exchanges - Transportation Assignments (Winter)	\$5.9M	X	✓	✓	Revenue
Total Transportation Exchanges - FT-RAM related						\$37.3M
Total All Transportation Exchanges						\$51.6M

In its evidence, Union provided detailed descriptions of each type of transaction listed in the table above and addressed whether the transaction relied on temporarily surplus assets, occurred on an unplanned basis and was sold as a service. This evidence is found at Exhibit B, Tab 2. Union also provided its rationale for treating the FT-RAM related transactions (Lines 4-7) as utility earnings in its Argument-in-Chief at pages 14-16.

Union argued that all of the FT-RAM related transactions rely on assets that are temporarily surplus to the needs of customers, occur on an unplanned basis and are sold as a service.

In regards to the Winter Assignment / Exchange Transactions (Line 7), Union noted that, typically, transactions of this type would not meet the criteria of temporary surplus as outlined by the Board. Union noted that this service is sold as a combination of transportation assignment and transportation exchange service. While on most days during this period there may be transportation that is temporarily surplus to the utility needs, at the time of sale, Union cannot be certain that a design day will not occur. On days where there is a design day, then there is no temporary surplus asset. Union noted that this is why Table 1 reflects an "X" in the relevant column.

However, Union noted that, in 2012, the overwhelming majority of the optimization activity which took place under this category related to optimization of the TCPL Empress to Union CDA contract (unlike prior years which involved the EDA). Union

noted that this contract serves a distinct purpose: while a South asset, on design day in Union North, the Union CDA contracted capacity is diverted upstream to serve Union North markets. As a result, there is, in fact, temporary surplus transportation capacity between Union North and the Union CDA. The risk that Union will be short of gas in the delivery area has been avoided because under the exchange, S&T arranges for the gas to be delivered during the winter exactly where it was intended under the gas supply plan (in Union North).<sup>11</sup>

Overall, Union argued that all revenues generated from FT-RAM related transactions are appropriately treated as utility earnings subject to earnings sharing under the terms of the IRM Framework.

### **Board Staff Submission**

The issue in the current case is fundamentally the same as the issue that was before the Board in Union's 2011 ESM proceeding. Board staff submits that it is incumbent upon the Board to consider the evidence before it now to assess whether there is any reasonable basis for the Board to depart from the decision and reasons rendered in the 2011 ESM case. The Board is not bound by the 2011 ESM decision.

The evidence before the Board in the 2011 proceeding led the Board to conclude that revenues generated from FT-RAM related transactions are properly classified as gas cost reductions (and should therefore be recorded in Account 179-130 – Upstream Transportation FT-RAM Optimization Deferral Account for sharing with ratepayers).

Board staff is of the view that in the current proceeding, Union provided better, more thorough and complete evidence explaining its FT-RAM related activities than it did in 2011. Board staff notes that there were also some changes to the activities undertaken by Union in 2012 as compared to 2011. In 2011, Union entered into some FT-RAM related assignments that occurred for an entire year.<sup>12</sup> In 2012, Union did not enter into any annual transactions.<sup>13</sup> In addition, in 2011, Union entered into some FT-RAM related Winter combined Assignment / Exchange transactions which were supported by capacity used to serve Union's EDA. This activity was greatly limited in 2012. Board staff submits that the combination of this more comprehensive evidence and the changes to Union's activities, could be a reasonable basis for the Board to make a decision in the current case which is different from the decision it made on the same issue in 2011.

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<sup>11</sup> Union Argument-in-Chief at pp. 15-16.

<sup>12</sup> Exhibit J1.8.

<sup>13</sup> Exhibit B, Tab 2 at p. 13.

The Board, in its EB-2012-0087 Decision and Order on Preliminary Issue, set out the following:

The Board finds that Union's evidence in the RP-2003-0063 / EB-2003-0087 proceeding, when taken as whole, does not support the conclusion that the planned optimization of gas supply related assets would be considered a transactional service. The evidence in the above noted proceeding explicitly speaks to the fact that with a balanced gas supply portfolio there will be few, if any, firm assets available to support transactional services on a future planned basis. In the Board's view, this statement speaks to the fact that the portion of utility gas supply assets that is available to support transactional service activities is only the portion of those assets that is temporarily surplus to the gas supply plan as a result of factors beyond Union's control.<sup>14</sup>

The Board's decision in Union's 2011 ESM proceeding essentially set out two criteria which need to be considered when determining whether revenues generated from capacity release transactions should be treated as Transactional Service revenues. These two criteria are as follows:

- 1) The transaction must rely on temporarily surplus assets.
- 2) The transaction must be unplanned.

Board staff is of the view that the first criterion, as set out by the Board, speaks to whether the assets supporting the transaction are required to serve customer needs on the day(s) that the transaction is in effect. If the assets are not required to serve customer needs at that time, the assets are properly considered temporarily surplus assets.

Board staff is of the view that the second criterion, as set out by the Board, relates to whether generating optimization opportunities is central to the development and management of the gas supply plan. If the utility's gas supply plan is right-sized and generating optimization activities are not part of the gas supply planning process, the transaction is properly considered unplanned.

Board staff is of the view that these two criteria are appropriate for considering whether revenues from FT-RAM related transactions should be treated as utility earnings or as gas cost reductions.

As noted previously, Union's gas supply plan supports Union's position that FT-RAM activities occur on an unplanned basis. There was no evidence filed to the contrary.

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<sup>14</sup> Decision and Order on Preliminary Issue, EB-2012-0087, p. 28.

In regards to whether the FT-RAM transactions rely on temporarily surplus assets, Board staff has separated its submission by transactions type.

Board staff is of the view that the Summer / Shoulder Month and Winter Exchange Transactions (Lines 4 and 5 in the table set out above) rely on temporarily surplus assets. Board staff notes that Union described in detail, in Section 12.1 of its application, the operation of these transactions. Board staff is convinced by this evidence which highlights the surplus assets that were used to support the transactions. As such, Board staff submits that the revenues associated with those transactions are appropriately treated as utility earnings in the context of Union's IRM Framework.

Board staff is of the view that, for the most part, the combined Assignment / Exchange transactions rely on assets temporarily surplus to the needs of Union's customers.

In regards to the Winter combined Assignment / Exchange transactions (Line 7 in the table set out above), Board staff notes that, in general, there would not be any temporarily surplus assets available to support these winter month transactions. As agreed to by Union, at the time of the sale of a Winter combined Assignment / Exchange transaction, Union cannot be certain that a design day will not occur. On a design day, there would not be any temporarily surplus assets available to support the transaction. However, Union noted that the majority of its Winter combined Assignment / Exchange transactions that took place in 2012 are related to the optimization of the TCPL Empress to Union CDA contract. Board staff submits that the unique nature of Union's use of this contract (as discussed previously) allows that, even on the design day, temporarily surplus assets would be available to support transactions that utilize this contract.<sup>15</sup> Board staff is convinced by Union's evidence that its 2012 Winter combined Assignment / Exchange transactions rely on assets that are temporarily surplus to the needs of Union's customers as they are supported by capacity on Union's CDA contract.

In regards to the Summer / Shoulder Month combined Assignment / Exchange transactions (Line 6 in the table set out above), Board staff is of the view that Union did have temporarily surplus capacity available in the summer months of 2012 to support these transactions. Board staff finds the evidence in Section 12.2 of Union's application which highlights the surplus assets that were used to support the transactions convincing. Therefore, Board staff submits that the revenues associated with those transactions are appropriately classified as Transactional Service revenues (and should be treated as utility earnings in the context of Union's IRM Framework).

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<sup>15</sup> Union Argument-in-Chief, pp. 15-16.

Board staff notes, however, that Union has included transactions that occur in March as part of the Summer / Shoulder Month combined Assignment / Exchange line item (Line 6 in the table above). Board staff is of the view that the month of March is properly considered a winter month. Board staff submits that, although unlikely, the design day could occur in March. As such, Board staff is of the view that the March combined Assignment / Exchange transactions are properly considered Winter combined Assignment / Exchange transactions. As noted previously, Board staff has no concerns with Winter combined Assignment / Exchange transactions that rely on the Empress to CDA contract (due to Union's unique use of that contract). However, Union noted that it did perform a combined Assignment / Exchange transaction for the month of March which included an assignment of Union's Empress to Union EDA capacity.<sup>16</sup> Board staff is of the view that at the time of sale, Union could not have known whether there would be surplus assets available to support the transaction. Therefore, Board staff is of the view that this transaction, which Union stated generated \$0.7M in revenues<sup>17</sup>, does not rely on temporarily surplus assets. Board staff is of the view that the revenues associated with the March combined Assignment / Exchange transaction (which included an assignment of Empress to EDA capacity) does not fall within the criteria set out by the Board for determining whether a transaction is properly considered a Transactional Service. As such, Board staff submits that the \$0.7M associated with this transaction should be properly classified as a gas cost reduction and should be shared 90:10 in favour of ratepayers through Account 179-130 (the Upstream Transportation FT-RAM Optimization Deferral Account).<sup>18</sup>

Board staff is of the view that, with the exception of the March combined Assignment / Exchange transaction (which included an assignment of Empress to EDA capacity), Union's 2012 FT-RAM related transactions occurred on an unplanned basis and relied on temporarily surplus transportation capacity. On that basis, Board staff submits that the revenues generated from Union's FT-RAM related transactions (with the exception of the \$0.7M generated from the March transaction discussed above) are properly considered Transactional Service revenues and should be recorded as utility earnings subject to earnings sharing in accordance with Union's IRM Framework.

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<sup>16</sup> Exhibit J2.1.

<sup>17</sup> Ibid.

<sup>18</sup> Board staff recognizes that treating the \$0.7M related to the March transaction as a gas cost reduction (as opposed to utility earnings) will not change the net amount collected from ratepayers (between the disposition of the deferral accounts and the earning sharing amount) as Union remains in the 90:10 earnings sharing bracket. This can be seen from Union's undertaking response in Exhibit J2.2. However, Board staff believes that, on a principled basis, this amount is best considered a gas cost reduction and allocated in the appropriate manner.

## Preparation of Audited Utility Financial Statements

In the EB-2011-0210 proceeding, the Board directed Union to prepare and file separate Audited Financial Statements (“AFSs”) for that portion of its business that is subject to rate regulation. In that proceeding, Union estimated the cost of preparing AFSs to be approximately \$400,000.

In the current Application, Union filed an Addendum to inform the Board that a more current estimate indicates that the costs of preparing AFSs for the regulated business was projected to increase from \$400,000 to \$1.3 million. In the Addendum, Union explained that this is a one-time cost comprised mainly of system related modifications. Union further noted that there would be an ongoing cost of \$80,000 for preparing the financial statements on an annual basis and indicated that it did not expect any material variation to this estimate.

In its Argument-in-Chief, Union noted that the parties advocating for separate audited financial statements in the EB-2011-0210 proceeding failed to identify any information not already disclosed by Union in that proceeding or by Union in response to the Board’s Reporting and Record Keeping Requirements (“RRRs”). Union submitted that it is unclear what incremental information would be made available to the Board and intervenors as a result of the Board’s directive. Union also stated its intention to seek recovery of the costs related to the audited financial statements from ratepayers through the deferral account established in EB-2010-0210.

Board staff agrees with Union that the information that would be provided in the AFSs is not incremental to the information filed in a rebasing rate application or information reported in the RRRs. That is not the issue. At issue is the rigour exercised and level of confidence provided in information that is used in establishing appropriate allocation between the rate regulated and non-rate regulated storage businesses. This confidence can be provided by an annual independent assessment of these allocations. This is particularly important because approximately 24% of Union’s Earnings before Interest and Tax (“EBIT”) for 2012 comes from Union’s unregulated business.<sup>19</sup>

Board staff submits that separate AFSs would be the ultimate means to achieve that goal. This is also consistent with Section 2.1.6 of the natural gas RRRs which require distributors to file separate financial statements for the rate regulated portion of the utility. Board staff also notes that in the EB-2010-0008 proceeding, Ontario Power Generation was required by the Board to file separate audited financial statements for the regulated portion of its business.

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<sup>19</sup> Union Gas Proceeding EB-2011-0210, Exhibit F4, Tab 2, Schedule 1

Board staff believes that filing AFSs for the regulated portion of the business will allow the Board to better assess revenue requirement and earnings sharing in rate applications and monitor performance during the IRM period. Further, the provision of information in a separate AFS for the regulated business will lead to greater transparency and improved efficiency in rate applications.

Were the Board to be concerned with the level of the revised cost estimate provided by Union to prepare the AFSs, Board staff submits that other options exist that would enhance the robustness of the financial information currently presented by Union. These options include an assurance provided by an independent professional advisor (an annual 3<sup>rd</sup> party assessment) regarding the required financial information (this may not necessarily be in the format of financial statements) or segmented note disclosure within Union's consolidated financial statements. While not as robust as a full separate set of AFSs as advocated by Board staff, Board staff submits that either option outlined above would be a significant improvement over the status quo. Unfortunately, there is nothing on the record from Union related to options and associated costs other than separate AFSs that could provide the greater assurance that Board staff has sought. .

#### **Deferral Clearing Variance Account No. 179-132**

Union requested approval of a deferral account to capture the difference between the balances approved for disposition and the amounts actually refunded to or recovered from ratepayers. Union submitted that prior to 2012, these differences were not material but this changed in 2013.

In its Argument-in-Chief, Union submitted that as a matter of principle, it would be inconsistent with the establishment of deferral accounts if Union, or ratepayers, were to gain or lose on the disposition of these account balances.

Board staff supports the establishment of this new deferral account as it will eliminate forecast error risk and ensure that all parties are held harmless as a result of the disposition process. Board staff also notes that this proposal is consistent with the approach used by Enbridge Gas Distribution as well as electricity distributors in Ontario.

All of which is respectfully submitted.