

ONTARIO ENERGY BOARD

IN THE MATTER OF an Application by Enbridge Gas Distribution Inc. for an order or orders approving or fixing rates for the sale, distribution, transmission and storage of gas commencing January 1, 2014.

FINAL ARGUMENT

Industrial Gas Users Association (IGUA)

1. The multi-year rate application which Enbridge Gas Distribution Inc. (EGD) has brought forward is a complicated one. In IGUA's view, needlessly so.
2. EGD has been less than transparent in constructing and advocating its proposal.
3. For example, the prefiled evidence and much of EGD's presentation of its case, both formally and informally, has needlessly conflated the Site Restoration Cost Proposal (SRC) with the presentation of revenue requirement/rates for the period from 2014 through 2018. The record now reveals that the two topics are related only insofar as the SRC proposal would, if accepted, mitigate the impact of EGD's rate proposal. It does not breach any confidences to state that much of the time spent in the Board mandated settlement conference was preoccupied with teasing out from the balance of the filing, and in particular from the revenue requirement/rate presentation, an understanding of the quantum and impact of the SRC proposal. IGUA has no doubt that this effort came at the expense of discussions on other important aspects of the application, none of which were ultimately resolved in the mandated discussions.
4. Another example of the lack of transparency in presentation and advocacy of this application is the inaccuracy, from the outset, of the characterization of the

proposal as a 5 year rate plan. Initially, the capital budgets were left open for 2017 and 2018, resulting in, at its highest, a 3 year rate plan. Upon reformulation of the proposal half way through, the capital budgets were nominally set for 2017 and 2018, but artificially so using 2016 levels and the addition of variance accounts for the two most significant, in terms of justification for a “custom incentive regulation” approach, capital expenditure areas; system integrity and relocation work. This approach did not result in a 5 year rate plan of the nature contemplated by the Board’s *Renewed Regulatory Framework for Electricity (RRFE)* on which EGD relies in advocating that its proposal is a “Custom Incentive Rate Plan”.

5. Throughout the process EGD has maintained that its forecast capital expenditure reflects a fundamental, structural shift in capital expenditure requirements during the proposed 5 year term of the rate plan, when in fact it appears to IGUA (and others) that when removing the impact of discrete, pre-approved capital projects, no such structural shift is apparent.
6. Other parties, notably including School Energy Coalition (SEC), Canadian Manufacturers and Exporters (CME), and Energy Probe (EP), will be filing extensive and detailed argument on various aspects and subtleties of EGD’s application.
7. IGUA has had the benefit of review, through counsel, of drafts of some of these filings. Given the comprehensive approach that these other ratepayer intervenors will be taking to this argument, IGUA defers on the details to them and will focus its own submissions more generally.
8. In doing so, IGUA would like to credit SEC’s counsel and Energy Probe’s (EP) Consultant (Mr. Aiken) in particular for their continued efforts to; i) engage in a full and detailed critical review of this very complex and in large measure opaque application; and ii) foster communication, including exchange of materials and draft submissions, with other parties. While IGUA does not necessarily endorse each argument and position advanced by SEC or EP, it does endorse many of

them and, in respect of all issues has benefitted, and believes that the Board will benefit, from SEC's the thorough and reasoned analysis presented on behalf of these intervenors.

9. IGUA herein offers brief submissions on the following topics:
 - a. EGD's SRC proposal.
 - b. Proper characterization of EGD's application.
 - c. EGD's asserted capital requirements.
 - d. EGD's Z-factor proposal.
 - e. Appropriate approvals and further directions.

SRC Proposal

10. IGUA endorses SEC's position on EGD's SRC proposal, as we understand a number of intervenors do.
11. IGUA anticipates that SEC's argument will provide a comprehensive analysis of the economic rationale for site restoration cost recovery, and IGUA has had the benefit of reviewing, through counsel, a number of drafts for that analysis.
12. IGUA agrees with SEC that:
 - a. The \$900 million collected by EGD from ratepayers over time on account of site restoration costs should be refunded to ratepayers, over time, and in a manner that avoids an abrupt upward rate adjustment following the last installment of such refund. SEC has proposed a 10 year refund schedule, which also preserves the ability to revisit the appropriateness of a site restoration provision at the next EGD rate rebasing should the Board determine it appropriate to do so. IGUA endorses this proposal.
 - b. Going forward, site restoration costs should be recovered as an in-year expense item, rather than a future looking provision.
 - c. To the extent that 2014 rates are set with reference to 2013 Board approved rates, an adjustment to the 2013 reference rates should be

made to remove \$61.6 million on account of replacement of SRC provision with operating expense treatment for site restoration activities.

13. IGUA has reviewed Board Staff's submissions on this topic, and is aware that Board Staff has argued against return to ratepayers of the \$900 million collected by EGD over the years on account of future site restoration costs. IGUA disagrees with Board Staff in this respect, and agrees with SEC that prior to re-establishment by the Board of any provision for asset abandonment or site restoration, a more careful review and determination of the proper purpose and appropriate mechanism for any such provision is required. In the event that such a review were determined by the Board to be warranted, it can be had between now and the next EGD rebasing without peril of over-refund (relative to any future provision determination) of costs already recovered from ratepayers.

Proper Characterization of EGD's Application

14. It has been, and remains, IGUA's view that applicants before this Board have both the privilege, and the obligation, to formulate their own rate proposals, and to request that the Board consider any such application on its own merits.
15. IGUA understands the Board's ratemaking policies, such as those arising from the *Natural Gas Forum* and the *RRFE*, to be guidance to rate regulated applicants regarding the application framework which the Board favours. Such policies do not bind individual Hearing Panels of the Board, and applicants should be free to advance, and seek to justify, alternative proposals which do not fit neatly into a pre-articulated Board policy.
16. In doing so, however, it is incumbent on the applicant to demonstrate why its application should be approved, and in particular why the Board should depart, in the particular circumstances of the application before it, from its pre-articulated policies. Such demonstration should be both persuasive and transparent.

17. IGUA agrees with those parties who will argue that EGD has neither been persuasive nor transparent in its application for what amounts to a 3 year cost of service and 2 year cost flow-through rate application.
18. While the Board's *RRFE* policy includes an expectation that a Custom Incentive Rate plan be of at least 5 years in duration, EGD's proposal essentially amounts to 3 years (2014 through 2016) of pre-set rates, followed by 2 years (2018-2019) in which rates would be set such that capital expenditure requirements central to final rates would be established on the basis of 2016 capital cost forecasts simply extended by two years and made subject to deferral account treatment for two main categories of capital expense (relocations and integrity expenditures). In the result capital expenditures in 2017 and 2018 would not be subject to the "incentive" contemplated in the *RRFE* policy for a Custom Incentive Rate plan.
19. While the *RRFE* policy on Custom Incentive Rates contemplates that benchmarking and the Board's own inflation and productivity analyses would provide critical inputs into determination of just and reasonable rates, EGD has not seriously addressed any of these additional parameters. It has simply provided cost of service forecasts which are essentially advocated as standing on their own to establish just and reasonable rates for 3 years, and partial rates for the next 2 years.
20. The *RRFE* policy further contemplates a comprehensive asset plan and associated capital budget. EGD's evidence has demonstrated that its asset planning approach is still very much a "work in progress" and does not in fact directly tie to, and support, its capital budget. (As already noted, there is no capital budget, *per se*, offered for 2018 and 2019.)
21. As has been submitted by Staff and as will be noted by others, EGD has embedded within its rate proposal "*multiple regulatory levers ... for the purpose of managing or eliminating risk*".¹ Such an approach is contrary to the spirit and

¹ Board Staff Submission, April 15, 2014, page 33.

intent of the Custom Incentive Regulation framework articulated as part of the *RRFE*, in which risk and reward to the utility are intended to go hand in hand.

22. IGUA endorses the following aspect of Staff's submission, which will be echoed in other submissions:²

"...in addition to filing a plan which gives the Board very little evidence on which to rely to satisfy itself that the forecasts of cost and revenues are reasonable, or at least within the range of reasonableness, Enbridge has asked for new deferral and variance accounts, one of which Enbridge has admitted is asymmetrical in favour of the utility, an expanded definition of what would qualify for Z-factor treatment, annual adjustments for a significant number of variables affecting revenues, projected ROE which changes annually, WACC that changes in every year of the plan, and variance account treatment for the large "extraordinary" capital items within the plan term.

....at a high level, Staff submits that there is not an appropriate balance of risk and reward in the Proposed Customized IR Plan as filed."

23. These concerns, and others like them, have led Staff, and will lead many other parties, to advocate that the Board should reject EGD's 5 year rate proposal. IGUA agrees. (The question of what the Board should then do is addressed at the conclusion of these submissions.)

EGD's Asserted Capital Requirements

24. One of the primary rationales offered by EGD for departure from a traditional I-X approach to rate setting in favour of what it (inappropriately) characterizes as a "Custom IR" rate model is an assertion of significantly large, multi-year capital investment requirements that exceed historical levels.
25. Energy Probe's argument will demonstrate that once the GTA Project and the Ottawa Project are stripped out of EGD's capital expenditure forecasts, the "core capital" expenditures remaining are forecast to follow a flat expense profile which

² Board Staff Submission, April 15, 2014, page 33.

completely aligns with actual 2013 capital expenditures and trends down relative to historical capital expenditures.

26. IGUA acknowledges that the GTA project and Ottawa project capital expenditures are significantly large. They are, however, discrete, already approved, and can be easily addressed through application of a pass through to revenue requirement (a “Y-factor”). This is the manner in which analogous (and contemporaneous) expenditures by Union for its approved expansion and reinforcement projects are being treated.
27. Further, EGD has not proposed any moderation of the large, GTA project and Ottawa project associated revenue requirement, as would be contemplated in a Custom IR Rate model.³
28. EGD has not established capital expenditure requirements that support a Custom IR Rate plan.
29. IGUA would acknowledge what it suspects underlies the obvious uncertainty that EGD has in respect of integrity costs in 2017 and beyond. While costs for the investigation now mandated by the TSSA pipeline integrity requirements should be neither unexpected nor difficult to forecast, costs for remediation which may be determined necessary following investigation might well be unexpected and difficult, or impossible, to forecast. IGUA is concerned about what remediation requirements and expenditures might ultimately be determined to be required. This issue should be revisited once the integrity investigations have been concluded, or at least are well underway (which was the approach for EGD’s initial capital expenditure forecast proposal).

³ Tr. 2, page 74, lines 23 – 25.

EGD's Z-factor Proposal

30. EGD has proposed changes to the z-factor framework for passing unexpected costs through a previously approved rate plan. One of the proposed changes is to adjust the wording related to the extent to which the cause of a cost increase (or decrease) is related to the utility undertaking.
31. The analogous provision agreed to with Union Gas, and endorsed by the Board, is worded as follows:⁴

...the cost increases/decreases must:

1. *causally relate to an external event that is beyond the control of utility's management;*
2. *result from, or relate to, a type of risk;*
 - a. *for which a prudent utility would not be expected to take risk mitigation steps; and*
 - b. *which is out of the realm of the basic undertaking of the utility (per EB-2011-0277 Decision, page 13); [Emphasis added.]*

32. EGD proposes wording that IGUA is concerned is unduly narrow:⁵

Management Control: The cause of the cost increase or decrease must be: (a) not reasonably within the control of utility management; and (b) a cause that utility management is unable to prevent by the exercise of due diligence.

33. The essential distinction between the approved Union wording and the proposed EGD wording is, in IGUA's view, clarity on the allocation of risk associated with the basic undertaking of the utility.
34. The EB-2011-0277 decision referred to within the text of the Union z-factor criteria was the EGD's 2012 rate application. The z-factor consideration in that application arose in respect of "cross-bores" or "sewer laterals". The expenses in

⁴ Exhibit K1.4, page 23 of the Union Settlement Agreement.

⁵ Ex. A2/T4/S1/p2.

issue were those incurred by EGD to manage circumstances in which trenchless installation of gas service laterals to a premises resulted in the gas pipe passing through a sewer pipe serving the premises. The result was a risk that a gas leak could result in gas entering the premises through the sewer connection.

35. In rejecting EGD's application for z-factor treatment of costs associated with identification and remediation of these situations, the Board articulated the notion of activities that were within the scope of *"the fundamental undertaking of the utility"*.⁶
36. In rejecting the z-factor claim advanced by EGD in that case, the Board determined that *"the risk management associated with the installation and maintenance of the distribution infrastructure as a whole within the franchise"* is part and parcel of the *"fundamental undertaking of the utility"*, which undertaking and associated risk management *"is precisely what the management of Enbridge is engaged in organizing and executing"*. The Board concluded that the cross-bore situation *"is precisely the kind of risk that a prudent utility would be fully engaged in managing and mitigating"*. This was one of the (two) bases on which the Board rejected the z-factor cost recovery sought by EGD.
37. EGD has indicated that it does not intend, by its proposed z-factor wording, to alter the risk allocation reflected in the EB-2011-0277 decision.⁷
38. IGUA thus submits that, for the sake of clarity and consistency, the Board approved wording for Union's z-factor criteria, which expressly reflects that risk allocation, should be adopted for EGD's z-factor criteria as well.
39. IGUA also endorses arguments of others that in the context of EGD's overall revenue requirement, and particularly in the context of allocation of risk and reward within an incentive regulation framework (if one is to be accepted), it would be appropriate to increase the z-factor materiality threshold from EGD's

⁶ EB-2011-0277 Decision, May 10, 2012, page 13.

⁷ Response to Undertaking J2.2.

proposed \$1.5 million to the \$4 million agreed to, and endorsed by the Board for, Union Gas.

Appropriate Approvals and Further Directions

40. These submissions by IGUA, and the submissions of others opposed to approval of EGD's application, beg the question of what the Board should do next.
41. In respect of the bigger issue of how the Board should set rates in the face of EGD's deficient application, various suggestions have been made.
 - a. Staff has suggested either maintaining current interim rates pending additional filings by EGD to address shortcomings in its application (including total cost benchmarking), or acceptance by the Board of a 5 year rate plan but imposition of additional productivity through imposing revenue reductions and reporting obligations.
 - b. Others will argue for imposition on EGD of an I-X rate setting plan, akin to that agreed to between Union and its stakeholders and subsequently endorsed by the Board.
 - c. Still other submissions will propose a host of discrete adjustments to various parameters of EGD's proposals.
42. As articulated at the outset of these submissions, IGUA believes that it is the privilege, and the obligation, of rate regulated applicants to bring forward transparent and justifiable rate proposals. IGUA thus recommends that:
 - a. Should the Board determine that it has a sufficient record upon which to set cost of service rates for 2014, it do so. EGD indicated in examination that would be a viable solution, pending redevelopment of a longer term rate plan if necessary⁸; and
 - b. The Board provide in its decision on this application guidance to EGD on the reasons why EGD's rate proposal is unacceptable, and what EGD should address before coming back with an alternate proposal for implementation in 2015 (and beyond).

⁸ Tr. 2, page 69, lines 22 through 28.

43. EGD can then consider the record in this proceeding, including the various suggestions for the path forward made in the arguments filed, and develop a proposal based on the Board's guidance and the reactions of stakeholders to the current application.
44. In doing so, IGUA would urge EGD to consider how to best plan for and budget for integrity expenditures once integrity investigations are well advanced and greater clarity on the scope and pace of such integrity expenditure requirements is possible.
45. In IGUA's submission, the Board should proceed with disposition of the SRC proposal in the interim and in the manner advocated by SEC but with one adjustment in respect of the method of refund to customers. As advocated above, the SRC issue is not related, except as to mitigative effect, to a prospective rate plan.
46. In respect of the adjustment to SEC's proposal, as the Board does with variance account clearances, contract customers should receive their refund in a lump sum rather than in a longer term rate rider. Particularly following the fuel price shocks of this past winter, such an approach would provide a salutary and appropriate gas cost mitigative effect for high-volume gas consumers. (The Board may wish to consider dividing such a credit into two installments, and deferring payment of the second of these installments pending determination of whether a site restoration or other abandonment cost provision will ultimately be required. This would avoid a sizeable contract customer credit only to be followed by a sizeable charge.)
47. IGUA would also endorse Staff's recommendation, regardless of the outcome of this application, that EGD institute an annual stakeholder meeting in a format similar to that agreed to by Union.⁹ Union has now held the first such meeting, at which we represented IGUA, and which we found to be very helpful both in

⁹ Board Staff Submission, April 15, 2014, page 70.

respect of general reporting and in respect of visibility into upcoming regulatory activity. Such a mechanism could be particularly useful to EGD should it seek to re-establish some consonance between its world view and that of intervenors and Board Staff.

48. In addition, Staff, intervenors, and EGD itself have all effectively proposed further consultation on development of an appropriate efficiency carryover mechanism to incent efficiency initiatives late in the term of an incentive regulation rate plan. IGUA endorses the concept of an efficiency carryover mechanism, and agrees with all of these parties that further work is required in development of an appropriate mechanism should one be brought forward.
49. Finally, Staff has proposed a further consultative review of the proposed Regulatory Cost Allocation Mechanism (RCAM) in determining the appropriate allocation of shared corporate costs to the regulated utility operations of EGD. IGUA endorses this recommendation as well.

ALL OF WHICH IS RESPECTFULLY SUBMITTED by:



GOWLING LAFLEUR HENDERSON LLP, per:
Ian A. Mondrow
Counsel to Industrial Gas Users Association

TOR_LAW\ 8414543\1