Ontario

ONTARIO ENERGY BOARD

OEB STAFF SUBMISSION

SETTLEMENT PROPOSAL AND DRAFT RATE ORDER

Union Gas Limited

Disposition of 2015 Deferral Account Balances and 2015 Earnings Sharing Amount

EB-2016-0118

July 13, 2016

Background

Union Gas Limited (Union) filed an application on April 19, 2016 with the Ontario Energy Board (OEB) for approval to dispose and recover certain 2015 deferral account balances. The application also seeks approval of the earnings sharing amount. Union noted that the earnings sharing amount is zero for 2015 as its utility earnings did not exceed the threshold which was established by the OEB as part of Union's 2014-2018 Incentive Regulation (IR) Framework.[1]

In Procedural Order No. 1, dated May 19, 2016, the OEB scheduled a Settlement Conference with the objective of reaching a settlement among the parties on all of the issues in the proceeding. The Settlement Conference was held on June 23 and 24, 2016.

Union filed a Settlement Proposal on July 7, 2016, which reflects full settlement on all the issues in the proceeding. Union attached the Draft Rate Order as an appendix to the Settlement Proposal.

OEB Staff Submission on Settlement Proposal and Draft Rate Order

OEB staff reviewed the Settlement Proposal filed by Union in the context of Union's 2014-2018 IR Framework[2], other applicable OEB policies, relevant OEB decisions, and the OEB's statutory obligations. OEB staff supports the Settlement Proposal as filed.

OEB staff is of the view that the Settlement Proposal appropriately reflects Union's 2014-2018 IR Framework. OEB staff submits that the OEB's approval of the Settlement Proposal is in the public interest and would result in just and reasonable rates for customers. OEB staff also submits that the accompanying explanation and rationale is adequate to support the Settlement Proposal.

OEB staff will provide comments on a few specific issues addressed in the Settlement Proposal below.

[1] EB-2013-0202.
[2] EB-2013-0202.

Deferral Accounts

As set out in Appendix C of the Draft Rate Order, the deferral account balances total to a $23.103 million debit to be collected from ratepayers (including interest to September 30, 2016).[3] This amount is higher than the cumulative deferral account balance in 2014 ($9.181 million).[4]

The large debit balance to be collected from ratepayers is largely driven by two accounts: (1) the Upstream Transportation Optimization Account (No. 179-131) which has a debit balance of $8.671 million; and (2) the Normalized Average Consumption (NAC) Account (No. 179-133) which has a debit balance of $10.634 million. There are smaller debit and credit balances in a number of Union's other deferral and variance accounts.[5]

The Upstream Transportation Optimization Account (No.179-131) was approved by the OEB in Union's 2013 Rebasing proceeding (EB-2011-0210). In its Decision and Order, the OEB directed Union to credit 90% of the forecasted optimization revenues to ratepayers in rates.[6] In accordance with the OEB's direction, Union credited $15.565 million in rates to ratepayers during 2015. However, Union earned only $7.739 million in net revenues from its upstream transportation optimization activities in 2015. Consequently, there is a debit balance in the account to be recovered from ratepayers, which is the difference between the amount in rates ($15.565 million) and 90% of the 2015 net optimization revenues ($6.965 million). Therefore, the total debit balance in the account is $8.6 million[7] ($8.671 million including interest to September 30, 2016).

The decrease in upstream transportation optimization revenue, between forecast and 2015 actual, is mainly as a result of: (1) the elimination of TransCanada PipeLines Limited's (TransCanada) Firm Transportation – Risk Alleviation Mechanism (FT-RAM) program;[8] and (2) a reduction in base exchange revenues due to customers committing

[3] The $23.103 million debit amount also includes a 2014 earnings sharing adjustment ($0.227 million credit to ratepayers) which is discussed at Section 21 of the Settlement Proposal. EB-2016-0118, Draft Rate Order, July 7, 2016 at Appendix C.
[4] EB-2015-0010, Decision and Rate Order, August 27, 2015 at Appendix C.
[5] EB-2016-0118, Draft Rate Order, July 7, 2016 at Appendix C.
[6] EB-2011-0210, Decision and Order, October 24, 2012 at pp. 39-40.
[7] EB-2016-0118, Corrected Pre-Filed Evidence, May 5, 2016 at Exhibit A, Tab 1, pp. 8-9.
[8] EB-2016-0118, Corrected Pre-Filed Evidence, May 5, 2016 at Exhibit A, Tab 1, p. 9.

to higher levels of Firm Transportation services on TransCanada which resulted in less market opportunities in the secondary market.[9]

OEB staff submits that the balance in the Upstream Transportation Optimization Account has been calculated appropriately in accordance with the methodology previously approved by the OEB.

The NAC Account (No. 179-133) uses the same methodology as agreed to by parties in the Settlement Agreement for Union's 2014-2018 IR Framework (EB-2013-0202) and as subsequently modified in Union's 2015 Rates proceeding (EB-2014-0271). The purpose of the NAC account is to record the variance in delivery revenue, storage revenue and storage costs resulting from the difference between the target NAC included in rates and the actual NAC for general service rate classes (Rate M1, Rate M2, Rate 01 and Rate 10).[10]

As noted in the Settlement Proposal, the NAC account had a credit balance of $1.554 million in 2014 and has a debit balance of $10.546 million in 2015. In the context of the large year-to-year change in the variance recorded in the NAC account, parties discussed whether Union's current methodology for forecasting NAC can accurately reflect: (1) the future impact of ongoing structural changes in gas consumption; and (2) the future impact of DSM savings. The parties agreed that, as part of Union's 2019 rebasing application, Union will file a study that assesses the appropriateness of its existing methodology for forecasting NAC. The study will allow for a consideration of potential changes, if necessary, to Union's NAC forecasting methodology in the future.[11]

OEB staff submits that the balance in the NAC account was calculated appropriately in accordance with the methodology previously approved by the OEB. OEB staff also supports the agreement that Union will file a study to assess the appropriateness of its existing methodology for forecasting NAC as part of its 2019 rebasing proceeding. In OEB staff's view, the filing of such a study in no way binds the OEB to continue with rate adjustments for NAC in 2019 and beyond.

Overall, OEB staff submits that the deferral and variance accounts conform to the accounting orders approved by the OEB and the balances in the accounts are

[9] EB-2016-0118, Union Interrogatory Responses, June 16, 2016 at Exhibit B.Staff.2 (b).
[10] EB-2016-0118, Corrected Pre-Filed Evidence, May 5, 2016 at Exhibit A, Tab 1, p. 22.
[11] EB-2016-0118, Settlement Proposal, July 7, 2016 at pp. 10-11.

calculated appropriately. Therefore, OEB staff supports the disposition of the account balances as agreed to by the parties in the Settlement Proposal.

Earnings Sharing

For 2015, there are no earnings to be shared with ratepayers as Union's utility earnings did not exceed the threshold for earnings sharing which was established by the OEB as part of Union's 2014-2018 IR Framework.[12] OEB staff submits that Union calculated its utility earnings for the purposes of earnings sharing correctly in accordance with previous OEB approvals.

OEB staff notes that, as part of the Settlement Proposal, Union agreed to credit ratepayers $0.227 million, which represents 50% of a $0.454 million adjustment to its 2014 earnings sharing calculation. Union recorded certain IT affiliate revenues and expenses in 2014 that were actually incurred in 2013.[13] If these affiliate revenues and expenses were properly recorded in 2013 (when they were incurred) instead of 2014, the earnings to be shared with ratepayers in 2014 would have been higher by $0.227 million (as Union was in a 50/50 earnings sharing position in 2014).[14]

OEB staff notes that Union's 2014 earnings sharing amount has already been approved and disposed to ratepayers on a final basis.[15] Therefore, the adjustment to the 2014 earnings sharing calculation, as agreed to by parties, is an out-of-period adjustment. However, OEB staff notes that the OEB has previously found that "an out-of-period adjustment can be justified if it ensures a utility does not profit on account of its own errors".[16] OEB staff submits that it is appropriate to refund the $0.227 million to ratepayers as it will ensure that Union does not profit from its own bookkeeping errors.

[12] The earnings sharing mechanism operates as follows: if the difference between the actual Return on Equity (ROE) and the benchmark ROE is greater than 100 basis points but less than 200 basis points, the excess earnings are shared 50/50 between Union and its ratepayers. If the difference between the actual ROE and the benchmark ROE exceeds 200 basis points, the excess over 200 basis points is shared 90/10 to the benefit of the ratepayers. For 2015, the benchmark ROE is 8.93% and Union's actual ROE from utility operations is 9.89%. Therefore, Union's actual 2015 ROE is 96 basis points above the 2015 benchmark ROE and the threshold for earnings sharing was not met. EB-2016-0118, Corrected Pre-Filed Evidence, May 5, 2016 at Exhibit A, Tab 2, pp. 4, 9 and Appendix B, Schedule 1.

[13] EB-2016-0118, Settlement Proposal, July 7, 2016 at p. 15.

[14] EB-2016-0118, Settlement Proposal, July 7, 2016 at Appendix A, Attachment 2; and EB-2015-0010, Exhibit A, Tab 2, Appendix B, Schedule 1.

[15] EB-2015-0010, Decision and Rate Order, August 27, 2015 at p. 3.

[16] EB-2014-0043, Decision and Order, April 10, 2014 at p. 2.

OEB staff also notes that the Settlement Proposal references Union's decision to consolidate data centre services with Spectra Energy Corporation (Spectra) and its other affiliates. The net impact on Union's 2015 earnings of charges from Spectra related to data centre co-location ($2.1 million) and charges to Spectra for the implementation of the data centre co-location initiative ($1.4 million) is $0.7 million. Therefore, this expense would not materially impact the earnings sharing results for 2015.[17]

However, Union stated that it expects that the impact of its decision to consolidate data centre services will be approximately USD$6 million in 2016 (less savings of $3 million in O&M expenses).[18] Therefore, Union's data centre consolidation initiative will likely have a more material impact on utility earnings in 2016. Union agreed to file evidence, as part of its 2016 Deferral Account Disposition and Earnings Sharing application, to explain its data centre consolidation decision. A list of the issues that will be addressed in Union's evidence is included as part of the Settlement Proposal.[19]

OEB staff supports the agreement to address the issue of Union's decision to consolidate data centre services with Spectra and its other affiliates as part of Union's 2016 Deferral Account Disposition and Earnings Sharing proceeding. OEB staff submits that the impact on 2015 earnings of Union's decision is not material and the issue is best addressed next year when the OEB and parties have more comprehensive evidence and the impact on earnings is larger.

Disposition of 2015 Deferral Account Balances and the Draft Rate Order

OEB staff supports Union's proposal to dispose of the balances in the deferral accounts prospectively over six months (October 1, 2016 to March 31, 2017) for general service rate classes. OEB staff also supports Union's proposal to dispose of the net 2015 delivery-related deferral account balances as a one-time adjustment with October 2016 bills for in-franchise contract and ex-franchise rate classes.[20] OEB staff submits that Union's proposed approach is consistent with previous OEB decisions.

[17] EB-2016-0118, Settlement Proposal, July 7, 2016 at pp. 15-16.
[18] Union noted that these amounts represent preliminary estimates and the actual costs and savings could be materially different.
[19] EB-2016-0118, Settlement Proposal, July 7, 2016 at pp. 16-17.
[20] EB-2016-0118, Settlement Proposal, July 7, 2016 at p. 18.

OEB staff also reviewed the Draft Rate Order attached to the Settlement Proposal. OEB staff submits that the Draft Rate Order accurately reflects the Settlement Proposal.

If the OEB were to approve the Settlement Proposal as filed, the impact on bills for typical residential customers in Union's North Service Areas for the six-month period from October 1, 2016 to March 31, 2017 is $19.54 (or approximately $3.26 per month on average over the 6 months). This represents an increase of about 2.3% on the total annual bill (based on Union's current OEB-approved rates effective July 1, 2016).[21]

The impact on bills for typical residential customers in Union's South Service Area for the six-month period from October 1, 2016 to March 31, 2017 is $7.12 (or approximately $1.19 per month on average over the 6 months). This represents an increase of about 1.1% on the total annual bill (based on Union's current OEB-approved rates effective July 1, 2016).

All of which is respectfully submitted.

[21] The annual bill used for this analysis is the average of the annual bills for the Fort Frances, Western, Northern and Eastern service areas.