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VIA COURIER

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor,
Toronto, Ontario M4P 1E4

Re: Comments of Enbridge Gas Distribution Inc. for Consultation on the Regulatory Treatment of Pensions and Other Post-Employment Benefit Costs

The following are the comments of Enbridge Gas Distribution Inc. ("Enbridge" or the "Company") in response to the Ontario Energy Board's ("OEB" or the "Board") Consultation and Follow-up Letter, dated August 10, 2016, seeking submissions on the "Consultation on the Regulatory Treatment of Pensions and Other Post-Employment Benefit ("OPEB") Costs, Board File Number EB-2015-0040".

Background

Enbridge provides a non-contributory basic pension plan that provides defined benefit or defined contribution pension benefits to the majority of its employees. The Company has two supplemental non-contributory defined benefit pension plans that provide pension benefits in excess of the basic plan for certain employees. The Company also provides OPEB for qualifying retired employees.

The accounting for Enbridge is governed by generally accepted accounting principles in the United States of America ("US GAAP"). Costs related to the period are expensed on an accrual basis.

Within its letter dated August 10, 2016, the OEB reminded stakeholders that the OEB had retained KPMG to provide technical support in relation to pension and OPEB issues, and that KPMG had prepared a report which was provided to stakeholders on May 19, 2016. The letter also indicated that at this time, the OEB would benefit from submissions on the following items:

- Principles that the OEB should adopt for purposes of assessing pension and OPEB costs in rate applications, including any principles the OEB should adopt in considering the appropriate rate mechanisms for cost recovery.

- Options for rate mechanisms for cost recovery.

- Views on whether a set-aside mechanism is necessary for pensions and OPEBs, if accrual accounting values were used for rate setting. The OEB is particularly interested in views on two of the options put forward by KPMG, reduction to rate base and a tracking account.

<u>Principles the OEB should adopt for assessing pension and OPEB costs</u>

One of the Board's stated objectives for the Consultation on the Regulatory Treatment of Pension and OPEB Costs is to determine what principles the Board should adopt for purposes of assessing such costs within rate applications, and in determining the appropriate rate mechanisms for cost recovery. Similar to Enbridge's earlier submission, Enbridge continues to support the development of guiding principles that the Board could consider in assessing the pension and OPEB costs, and rate recovery mechanism, for each of its regulated entities. Enbridge does not support that such principles be prescriptive and applied to each regulated entity given the variety of circumstances for each entity's pension and OPEB plans related requirements and impacts.

Throughout the course of this consultation, numerous principles have been identified by the Board and interested parties; some of which have more relevance than others in the determination of pension and OPEB costs and rate recovery mechanisms. Enbridge's thoughts on a number of principles are provided below.

- *<u>Fairness</u>* – In the context of this consultation, Enbridge sees fairness having two contextual meanings:
    1. The allocation of costs between current versus future ratepayers (intergenerational inequity), or
    2. Balancing the effects between ratepayers and the utility (i.e. the opportunity for the regulated entity to recover its prudently incurred costs).

  In either case, Enbridge believes fairness to be a relevant principle.

- *<u>Minimize intergenerational inequity</u>* – Refers to the concept that costs pertaining to a certain period should be recovered through rates (from customers) for that period and not through rates (from customers) for another period. Enbridge believes that this is a very important principle to be considered in the context of this consultation, and that to the extent possible, intergenerational inequity should be avoided. In addition to minimizing intergenerational inequity, it has also been noted during this consultation, that recovering costs in the correct period also sends appropriate price signals.

- *<u>Minimize rate volatility / stable cost levels</u>* – Enbridge believes that rate stability has some relevance within the context of this consultation, but may not be as relevant as other principles. Rate stability at the aggregate level (i.e. revenue requirement) is certainly a desirable outcome. Insofar that the stability of a particular cost component of revenue requirement, such as pension and OPEB costs, can aid in achieving rate stability, it is a consideration.

- *Standardization/consistency of regulatory mechanisms across gas and electricity sectors* – As stated earlier, given the unique circumstances of each regulated entity, Enbridge does not believe that a standardized pension and OPEB regulatory recovery mechanism, for the gas and electric sectors, is necessarily practical or appropriate. Utility specific circumstances must be able to be accommodated.

- *Pension and OPEB costs which are comparable as measured by other benchmarks* – Enbridge does not believe that the benchmarking of pensions and OPEB costs is an appropriate principle to be adopted in assessing such costs or the appropriate recovery mechanism. As indicated in Enbridge's earlier submission, and by many participants to this consultation, pension and OPEB costs are only two of the elements that make up an entity's total compensation package. The unique facts and circumstances of each entity may have differing influences on the components of their compensation plans. As a result, benchmarking would be more relevant at the total compensation or total cost level.

- *Ensuring the most efficient level of costs for ratepayers* – As indicated in its earlier submission, Enbridge does not believe this is a principle that is appropriately applicable to pension and OPEB costs, any more so than any other costs. Pension and OPEB costs are one type of costs that makes up a utility's request for annual revenue requirement that are recovered in rates paid by the customer. One interpretation of this principle could be that only the absolute lowest level of pension and OPEB costs, compared to all entities in Ontario who pay such costs, are to be paid to regulated entity employees and recovered from ratepayers. A guiding principle of the regulated tribunal process is for the OEB to determine just and reasonable rates. This determination is made not on any one individual cost but rather the impact of all costs that make up a utility's revenue requirement. Therefore, efficiency should be determined at the aggregate cost level and not at the cost element of pensions and OPEB. This interpretation could result in the regulated entities not being able to attract talented resources to perform at the same level of effectiveness as those currently employed, perhaps reducing the overall efficiency of the regulated entity. In addition, this interpretation could also be viewed as putting regulated entities that operate in larger areas such as Toronto at a disadvantage as compared to entities that operate in smaller communities where the cost of living is lower.

- *Minimize regulatory/administrative burden* – Enbridge believes that the minimization of regulatory and administrative burden is always a relevant principle as a higher burden generally results in increased costs to ratepayers.

This is no different when assessing pension and OPEB costs within rate applications. Any additional administrative burden creates additional complexity, requiring more time to evaluate and higher costs to administer, as well as higher costs to prepare for, evaluate, and conclude on a rate application. This would consequently mean higher costs to the ratepayers.

- *Alignment of regulatory mechanisms with accounting requirements* – Enbridge believes that alignment between regulatory mechanisms and accounting requirements is a relevant and appropriate principle to be considered in the assessment of pension and OPEB costs and recovery mechanisms. Consistency with accounting requirements would in many instances be simple to employ as this would likely be no change from the existing practice and result in less administrative and regulatory burden given one set of books, forecasts, external audit opinions, etc. It would also result in understandable results with less confusion and uncertainty, as interested parties such as investors and the auditors would be familiar with the methodology employed.

Having considered the identified principles, Enbridge believes that the most relevant or appropriate to serve as guiding principles in the determination of pension and OPEB costs and their associated rate recovery mechanisms are: ***fairness, the minimization of intergenerational inequity, the minimization of regulatory/administrative burden, and alignment with accounting requirements***.

As stated earlier however, adoption of these principles should not result in the same rate recovery mechanism for all regulated entities, given the unique circumstances of each regulated entity.

Appropriate method for cost recovery

With respect to pensions and OPEB, the accrual basis of accounting under US GAAP matches the expense to the proper time period in which the costs are incurred. Overall, Enbridge believes that the US GAAP accrual basis is most aligned with the principles of fairness, the minimization of intergenerational inequity, stability, and alignment with accounting requirements noted above. Therefore, accrual accounting under US GAAP is the most appropriate basis for Enbridge to recover its pensions and OPEB costs from customers.

There are several factors as to why Enbridge believes accrual accounting is the most appropriate:

- For Enbridge, the accrual basis is much less volatile compared to cash contributions, and provides for stable costs. Over the entire life span of a pension or OPEB plan, the total cash funding costs and accrual costs would be similar.

- The accrual basis of accounting is inter-generationally equitable, and therefore the customers will be paying for that particular year's cost.

- The accrual basis is aligned with the accounting treatment under US GAAP standards and would not require additional administrative burden to keep track of two sets of books, and there is uniformity given US GAAP is widely accepted.

- Recovering costs on the accrual basis is largely aligned with industry practices and other utilities.

- The KPMG report introduced, as a possible alternative approach, the Modified Funding Contribution method which Enbridge believes has several setbacks, as it is administratively burdensome, may not meet US GAAP requirements for regulatory offset, creates inter-generational inequities, and is inconsistent with accounting rules, which requires accrual accounting.

- Enbridge believes that the accrual approach provides the best balance of the guiding principles as compared to cost recovery on a cash funding basis. This is especially true when considering solvency funding requirements currently imposed on the registered pension plan by Ontario's *Pension Benefits Act*. Solvency funding introduces significant volatility and a greater risk of intergenerational inequity to cost recovery on a cash basis. The Ontario Ministry of Finance is currently reviewing the solvency funding framework, which may result in changes; any consideration of the cash funding basis, or the modified funding contribution method should wait until after a new funding framework is in place.

<u>Is a Set-Aside Mechanism necessary for cost recovery?</u>

Enbridge's understanding of the internally segregated account and retirement compensation arrangement approaches to establishing a set-aside mechanism, whereby pension and OPEB amounts collected from ratepayers in excess of amounts contributed to the plan, would require an entity to setup new processes and possibly segregate the funds and manage them. This would add administrative costs. Under this mechanism, each utility would need to establish new internal processes to track amounts and processes to keep the funds segregated, would require additional governance. If the funds are in a trust, there would be additional third party costs. Overall, internally or externally segregating the funds would not be a good use of these funds. Furthermore, the OEB will need a provision for utilities' additional costs from the increased administration costs and in turn would likely offset the benefit of having these costs segregated. This would also violate the principle to minimize regulatory/ administrative burden.

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Applicability of using "reduction to rate base" or a "tracking account"

Two other potential set-aside mechanisms identified by KPMG involve tracking the variance between accrual based recoveries and cash funding amounts, and either reflecting that variance as an element of rate base which would attract the weighted average cost of capital, or monitoring the amount through a separate "tracking account" that could attract interest.

Enbridge believes a reduction to rate base or an interest bearing tracking account is not necessary until such time as a problem has been identified. However, if the Board determines that through this generic proceeding a set-aside mechanism is a necessary tool for their review of pensions and OPEBs, then Enbridge believes the use of a tracking account would be preferable. The tracking account would allow the OEB to review the utility's variance between amounts recovered in rates versus amounts contributed. Should a Board Panel through a review determine that further action is required, such as tracking the variances, then that Board Panel should determine the appropriate rate to be applied to the balance.

In general, Enbridge believes that aligning with the OEB stated goal of following a principled approach, the OEB should monitor each utility and use the rate application review process to determine if utility-specific action is needed for the treatment of pensions and OPEBs. The set-aside mechanisms should be reviewed on a case-by-case basis, depending on each utility's circumstance. All of the proposed treatments being considered by the OEB in this proceeding should be applied in a symmetrical manner where there are payable or receivable situations with a utility's pensions and OPEBs.

Summary

The pension and OPEB cost questions / issues which the Board is seeking submissions about, involve complex financial, rate, and tax related issues. Enbridge submits that the current rate setting application process provides the OEB substantial opportunity to scrutinize a utility's proposed treatment of their pension and OPEB cost recovery requests and how that utility's pension plan is being managed. Establishing a standard prescriptive approach for all utilities, in how they should treat pensions and OPEBs, will result in transitional issues and additional costs to ratepayers.

Should you have any questions regarding this submission, please feel free to contact me or Andrew Mandyam at 416-495-6350.

Yours truly,

(Original signed)

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Cc: Andrew Mandyam, Director of Regulatory Affairs, Enbridge Gas Distribution Inc.