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June 16, 2017

Kirsten Walli, Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge Street
Toronto ON M4P 1E4

VIA EMAIL

Dear Ms. Walli,

Re: EB-2016-0351 – Natural Resource Gas Limited (NRG)
Application for approval to sell natural gas distribution system
Final Arguments of Vulnerable Energy Consumers Coalition (VECC)

Please find enclosed the final submissions of the Vulnerable Energy Consumers Coalition (VECC) in the above-referenced proceeding. We have also directed a copy of the same to the Applicant.

Best regards,

[*original signed*]

Cynthia Khoo
Counsel to VECC

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EB-2016-0351

ONTARIO ENERGY BOARD

Natural Resource Gas Limited

Application for Approval to Sell Natural Gas Distribution System

Final Submission
of the
Vulnerable Energy Consumers Coalition
(VECC)

16 June 2017

Cynthia Khoo, Counsel for
Vulnerable Energy Consumers Coalition

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1. Qualification of EPCOR to Operate NRG

1.1 In this application, EPCOR Natural Gas Limited Partnership ("EPCOR") proposes to purchase Natural Resource Gas Limited ("NRG"). EPCOR is an Ontario limited partnership and a wholly owned, indirect subsidiary of EPCOR Utilities Inc. ("EUI"). EUI is a holding company that conducts business through subsidiaries. The general partner of EPCOR is EPCOR Ontario Utilities Inc., and the sole limited partner is EPCOR Power Development Corporation. Both of these entities are subsidiaries of EUI. EPCOR Ontario Utilities Inc., as general partner, controls and has full and exclusive authority over the management and day-to-day operations of EPCOR. EPCOR Power Development Corporation is a limited partner that has an economic interest in the partnership, but will not play a role in the day-to-day operations and management of EPCOR.[1]

1.2 In response to VECC inquiring as to how this structure might differ in terms of responsibilities or liabilities arising from the current NRG ownership structure, EPCOR replied that it "will be subject to the same responsibilities and liabilities to utility customers as NRG currently is."[2] Specifically, current NRG customers will not be exposed to any risks under the proposed expansion by EPCOR Southern Bruce Gas Inc. EPCOR and EPCOR Southern Bruce Gas Inc. are separate legal entities and their liabilities and assets are not comingled.[3]

Human Resources

1.3 Through wholly owned subsidiaries, EUI builds, owns and operates electric transmission and distribution systems, and water and wastewater treatment facilities and infrastructure, providing related energy services across Canada and the United States. EUI and EPCOR do not currently own any natural gas distribution operations. However, NRG's general manager, as well as its operations and administrative personnel, will continue employment with EPCOR, allowing for continuity of service.[4] Specifically, EPCOR states:

> EPCOR intends on maintaining existing NRG management unchanged up to and including the general manager level. NRG's current President, Anthony Graat, will not be employed by EPCOR, nor will the two Co-Chairs. After the closing of the proposed sale transaction, the general manager will report to EUI's Senior Vice President, Commercial Services, Steve Stanley who has over ten years of experience running regulated utilities.[5]

1.4 In our submission, EPCOR will have the human resources capable of successfully continuing to safely serve the customers of NRG.

Credit and Capital

1.5 EPCOR's parent company, EUI, is a public issuer of debt with current credit ratings of A- (S&P) and A (low) stable (DBRS). EUI has credit facilities totaling $575 million, of which $350 million is available for borrowing. EUI also has the ability to issue long-term debt in the Canadian public debt market through an existing $1 billion, short-form base shelf

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1 Exhibit 1, Tab 1, Schedule 1, page 1.
2 NRG IRR VECC-1.
3 NRG IRR 1-IGPC-3.
4 NRG IRR 1-Staff-15 & VECC-4.
5 NRG IRR VECC-4.

prospectus, of which the entire $1 billion capacity is presently available.[6]

1.6 The evidence states,

> [T]he long-term debt costs of EPCOR, reflective of EPCOR's creditworthiness, may be modestly lower than NRG's cost of debt."[7] It is EPCOR's intention to apply market interest rates to its debt structure. Furthermore, "[I]t is EUI's practice that the material terms of an inter-company note payable will be comparable to lending agreements with third party financial institutions at the time the funding is to occur.[8]

1.7 If approved, the transaction will have the benefit of eliminating NRG's retractable class of shares. This would have the benefit of reducing NRG's financial risk. It would also simplify setting the appropriate capital structure for the purpose of ratemaking.[9]

1.8 In our submission, the resources available to EPCOR from EUI are sufficiently robust to satisfy the future capital requirements of NRG.[10] EPCOR possesses both the financial and managerial-staff resources to ensure the reliable, safe and efficient ongoing operation of NRG.

2. Rate Impacts

2.1 The estimated net book value of the Purchased Assets is $14,579,723, consisting of $1,584,392 in non-fixed assets (accounts receivable, inventory and recoverable-through-rates assets) and $12,995,331 in fixed assets. The purchase price of approximately $21 million is subject to final adjustments as outlined in the Asset Purchase Agreement and is greater than NRG's net book value.

2.2 EPCOR has stated that it will not seek to increase its future revenue requirement in order to recover these transaction costs.[11] EUI's current practice is to not record any premiums in the regulatory books for its regulated utilities, as the premium does not form part of rate base.

2.3 EPCOR has further stated that:

> EPCOR has reviewed NRG's rate application and expects that, based on EPCOR's anticipated cost structure, individual cost categories may be impacted but the total revenue requirement will be in line with that presented in the rate application. As such, the costs to serve NRG's customers under EPCOR are not expected to be higher than they otherwise would have been with NRG.[12]

2.4 In fact, EPCOR expects some benefits to customers based on its corporate procurement economies of scale in the areas of information technology, regulatory and legal costs, and potentially lower debt costs than that incurred by the current owners. However, some of these costs may be offset by increased compensation costs.[13]

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6 Exhibit 1, Tab 1, Schedule 4, page 4.
7 NRG IRR VECC-2.
8 NRG IRR 1-Staff-6.
9 Exhibit 1, Tab 1, Schedule 4, page 6.
10 See for example NRG IRR 1-Staff-5.
11 Exhibit 1, Tab 1, Schedule 2, page 2.
12 NRG IRR 1-Staff-1.
13 See for example, NRG IRR 1-Staff-2 and Union Gas-2

2.5 EPCOR intends to proceed with a five-year incentive rate application and will assume responsibility for seeing through EB-2016-0236 (to which VECC is a party). EPCOR has stated that it will file an amended application within six to nine months of the closing of the Asset Purchase Agreement. The application will be amended to reflect EPCOR's ownership of the system. NRG proposes to continue applying its interim Board-approved rates, which became effective October 1, 2016. The estimated monthly amount of unrecovered rate revenue for each month is $80,727.[14]

2.6 The application for purchase has caused a significant delay in NRG's current rate application. NRG filed its rate application on August 12, 2016. The Board issued its first procedural order (allowing for interrogatories) on September 28, 2016. It is unlikely that a revised application (as EPCOR has stated its intentions to submit) will come before the Board before August 2017, or at least one year since the original filing. At this point, we presume the Board will need to re-establish a procedure for discovery of the revised application. At a cost of approximately $81,000 per month, the resulting retroactive adjustment to rates for existing NRG ratepayers would be significant.

2.7 VECC intends to remain a party to the rate application in EB-2016-0236. The issue of retroactivity (within the meaning of interim rates) will be an issue in that proceeding, as will be the role of this application in prolonging the period for which interim rates have been in place. In our submission, if the Board grants leave to proceed with this transaction, it should make clear that EPCOR will be at risk for any amounts that may be determined to be unrecoverable as part of the delay that this current application caused to the EB-2016-0236 application.

2.8 The utility has put forward a reasonably cautious view of the benefits and costs of new ownership. On balance, we believe it has met the burden of proof in demonstrating no harm with respect to future distribution rates. With the proviso raised in paragraph 2.7 and based on the expectation that EPCOR raises no objection to the current standing of VECC in EB-2016-0236, we have no concerns with the Applicant's proposal.

3. Related Transactions

3.1 There are two material "inheritances" that EPCOR will receive from NRG as part of this transaction. First, EPCOR will continue to receive regulatory services from Ayerswood Development Corp. and for a period of 18 months after the close of the sale transaction. Second, EPCOR will also purchase natural gas from NRG Corp[15].

Ayerswood Development Corp.

3.2 VECC has no concerns with the continued use of Ayerswood Development regulatory services. However, the applicant should be aware that the cost of that service to be included in rates has been, and we expect will continue to be, an unresolved issue.

[14] NRG IRR VECC-3.
[15] NRG IRR 1-Staff-11.

NRG Corp. and SNC Lavalin System Integrity Study

3.3 While VECC is satisfied that EPCOR has met the no harm test with respect to distribution rates, the same cannot be said for gas costs. NRG Corp. is a related company to NRG with gas production wells in NRG's service territory. At present, these wells provide local supply to NRG's gas distribution system.

3.4 At NRG's last rebasing proceeding (EB-2010-0018), the utility was directed to retain an independent consultant to carry out a system integrity study to, in part, determine how much natural gas NRG required from NRG Corp. to address system integrity issues. This study was completed by SNC Lavalin and has been filed in the current rate application. Both in the EB-2016-0236 evidence and in response to interrogatories in this application, the current and potential new owners of NRG have presented their views regarding the necessity of obtaining ongoing gas supplies from NRG Corp, which have traditionally been substantially above market prices.[16] The issue of gas costs emanating from NRG Corp. is therefore central to EB-2016-0236.

3.5 EPCOR is not purchasing the gas production wells of NRG Corp. It has negotiated the right of first refusal upon NRG Corp.'s existing wells if NRG Corp. wishes to sell the wells to a third party during the term. EPCOR also has an additional option to purchase the wells during the term. In any event, however, EPCOR is here committing to purchase NRG Corp. As a condition to closing, NRG and EPCOR must enter into a gas purchase agreement,[17] according to which NRG Corp. is to use best efforts to supply a minimum volume of 17,657 Mcf annually.[18]

3.6 If this application is approved, EPCOR states that it intends to further review the findings and recommendations from the System Integrity Study completed by SNC-Lavalin and, if appropriate, complete additional analysis or studies as required to develop a comprehensive system integrity plan. EPCOR also states that its plans for the long-term supply of natural gas from NRG Corp. will be dependent on the outcome of this review.[19]

3.7 The system integrity study confirmed that on peak days, NRG's distribution system requires gas from wells within or near its distribution system to maintain system integrity. It also found that determination of a precise quantity of "required" system integrity gas was not possible. NRG and EPCOR appear to believe that either only NRG Corp. can provide the necessary gas, or that this supply of gas is the only solution to the system integrity issues, as opposed to new infrastructure. However, Tribute/ON have extensive pipelines in the area, including a high-pressure pipeline connected to a 700 psi Union Gas mainline. Tribute states that it would be pleased provide additional system supply capacity to the EPCOR system.[20]

3.8 The Board has yet to consider evidence on this issue provided in EB-2016-0236, including the SNC-Lavalin study, in addition to the competitive market study by Dr. Walsh. VECC previously asked a number of interrogatories on these studies as part of EB-2016-0236 (in November 2016), and these interrogatories remain unanswered.

3.9 Given the above, the Board should caution EPCOR regarding the risk associated with

[16] NRG IRR 1-Staff-4
[17] NRG IRR- VECC-5.
[18] NRG IRR 1-Staff-4.
[19] *Ibid*.
[20] Tribute Argument (2 June 2017).

inheriting “system integrity”-related gas. It is conceivable that the Board may find that NRG (EPCOR) has prudent alternatives to NRG Corp. market premium natural gas. If so, EPCOR would be at risk for any long-term contracting that might inhibit its ability to meet the needs of the utility’s ratepayers in the most cost-efficient way available.

4. NRG – Union Gas Penalties

4.1 Union Gas Limited (“Union”) assessed NRG a penalty for failing to balance gas in the winter of 2013-14. In a subsequent review of this penalty (under files EB-2014-0053, EB-2014-0361, and EB-2015-0044), the Board rendered a decision confirming a penalty amount of $1,106,016. To date, NRG has paid $399,453. EPCOR is not assuming the penalty payment obligation.[21]

4.2 NRG had argued that the penalty should be collected from its ratepayers. However, the Board found otherwise:

> The OEB finds that it would not be reasonable for NRG’s system supply customers to be burdened with the penalty costs, which were incurred as a result of insufficient care and attention given by NRG to its gas supply requirements over the 2013-2014 winter. As will be discussed further in Chapter 5, NRG’s actions were not prudent. As such, the OEB will ensure that the interests of NRG’s ratepayers will be protected with respect to the price of gas service by apportioning some of the costs resulting from the application of the penalty charge to NRG’s shareholder.[22]

4.3 In our submission, the payment is clearly to be borne by the shareholders of NRG. Since EPCOR is assuming none of the liability with respect to this matter, any issue of failure to make full payment would become a matter between Union and NRG. If full payment were not made, the only regulatory remedy left available would be for Union Gas to seek to recover the bad debt either from its own ratepayers or from the ratepayers of EPCOR. We do not think either of these potential remedies to be proper or fitting of the Board’s prior decision. Either would certainly cause the transaction to fail the “no-harm” test.

4.4 As such, in our submission, the Board should consider whether it should amend its order in EB-2014-0053 / EB-2014-0361 / EB-2015-0044 such that the balance of the penalty must be paid at the time of this transaction. In the alternative, the Board could make the approval of the proposal conditional upon EPCOR’s shareholders assuming the shareholder obligation of NRG. Presumably, in the event that occurred, the parties would renegotiate the price of the sale to incorporate this change.

5.0 Costs

5.1 VECC submits that its participation in this proceeding has been focused and responsible. Accordingly, VECC requests an award of costs in the amount of 100% of its reasonably-incurred fees and disbursements.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

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[21] NRG IRR Union Gas-1.

[22] EB-2014/0053/EB-2014-0361/EB-2015-0044, Decision and Order Natural Resource Gas Limited (NRG) (14 January 2016), page 15.