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VIA RESS, EMAIL & COURIER

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
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Attention: Kirsten Walli,
Board Secretary

Dear Ms. Walli:

Re: EB-2017-0306: Enbridge Gas Distribution Inc. and Union Gas Limited MAAD Application

Comments on the Intervenors' Draft Issues List

As BOMA indicated to the Board in its letter dated Friday, January 19, 2018, BOMA is supportive of the proposed Issues List for EB-2017-0306, attached to Ian Mondrow's letter of January 19, 2018. BOMA adds the following comments to provide additional context for its views on the appropriateness of the intervenors' proposed list, and EGD's submission filed on Friday, January 19, 2018, which dealt with its proposed draft Issues List and the intervenors' proposed Issues List.

BOMA is strongly of the view that the Board's Merger Policy contained in Rate-making Associated with Distributor Consolidation, Report of the Board ("2007 Report") and EB-2014-0138, Report of the Board, Rate-making Associated with Distributor Consolidation dated March 26, 2015 ("2015 Report"), do not, and should not, apply to the natural gas sector for several reasons. These documents deal with the electricity sector. In the Introduction of the July 2007 Report, it stated:

> *"Earlier this year, the Board initiated a consultative process focusing on the regulatory treatment of certain rate-related issues associated with consolidation in the electricity distribution sector. The purpose of the consultation was to assist the Board in developing a policy framework on relevant rate-making issues and to provide greater predictability for distributors and other stakeholders in relation to those issues."* (our emphasis)

And further stated (p1):

> *"The Discussion Paper identified, and stakeholders have confirmed, the following as principal rate-making issues warranting consideration by the Board at this time:*
>
> • *the timing for rate rebasing;*
>
> • *whether rate recovery of transaction costs should be allowed;*
>
> • *whether efficiency savings resulting from consolidation accrue to the shareholder, ratepayers, or both; and*
>
> • *whether the Board should require rate harmonization.*
>
> *This Report sets out the Board's policy on each of these rate-making issues in the context of certain transactions in the electricity distribution sector. Application of the policy will create a more predictable regulatory environment for distributors that are considering consolidation, thereby facilitating planning and decision-making and assisting distributors in determining the value of consolidation transactions. The Board's approach as set out in this Report builds on and complements the work of the Board in relation to incentive regulation, and addresses the issues in a manner that does not unnecessarily increase the regulatory burden on distributors or other interested parties. "*

In the 2015 Report, in the Introduction, the Board stated (p4):

> *"After considering the government's policy expectations, the results of the consultations, and the OEB's own expectations that the distribution sector should continue to seek out efficiencies especially through consolidation, the OEB has concluded that it will proceed at this time with amendments to its rate-making policy associated with electricity distributor consolidation."* (our emphasis)

And further stated (p3):

> *"The report of the Ontario Distribution Sector Review Panel, issued in December 2012, set out a vision for consolidation resulting in the less costly and more efficient delivery of electricity, with a predicted cost savings of $1.2 billion over the next ten years. When the Minister of Energy responded to the Panel's report, he indicated that he expected that the sector would find ways to achieve those savings through more efficient service delivery, including negotiated consolidations. This view was carried forward in the government's December 2013 Long Term Energy Plan ("LTEP"), where it is stated that the government expects electricity distributors to pursue innovative partnerships and transformative initiatives that will result in savings for electricity ratepayers. On March 31, 2014, the OEB issued a OEB staff Discussion Paper (the "Discussion Paper") providing background on the current policies, summarizing stakeholder input received in relation to those policies, and setting out questions for stakeholder comment with respect to potential changes to those policies. On November 13, 2014, the Advisory Council on Government Assets issued its findings which included the view that consolidation was needed to encourage modernization of the electricity distribution system."*

These documents are clear on their face that they apply only to the electricity sector.

The Board's merger policy, contained in the two Reports, were developed in the context of several important realities, including the fact that as of the time the restructuring of the industry in 1998, there were more than 300 electricity distributors in Ontario, many of them very small. Second, Ontario Government policy, from the beginning, supported the consolidation of the electricity distribution industry into fewer larger utilities, and that policy continues to this day. Both the reports of the Ontario Distribution Sector Review Panel in December 2012 and the November 13, 2014 Advisory Council on Government Assets were strongly supportive of

electricity distribution utility consolidations, citing the potential economies of scale, lower financing costs, more capacity for innovation, among other factors.

In order to provide a strong incentive for electricity utilities to consolidate, the Board's 2007 Report allowed the merged entity to defer rebasing for ratemaking purposes for up to five years to offset the merging utilities' "transactional" costs and "integration" costs. In other words, the utilities were permitted to retain 100% of any savings due to efficiencies or productivity improvements they were able to achieve, as a result of the merger, for a five-year period following the merger. The Board, in the 2007 Report, did not limit the incentive to the amount required to allow the utilities to recover their "transactional" and "integration" costs, but instead allowed the utilities to earn higher than normal profits (higher return on equity than the then approved Board approved rate) over the deferral period.

However, the electric utilities complained that they did not still have enough incentive to merge, and in the 2015 Report, the Board extended the "deferred rebasing period", during which the utilities could keep the savings, up to ten years, to offset transaction costs, integration costs, and to earn profits above those authorized by the Board's then ROE policy. The utilities had only to request ten years, and they were given it (see, for example, the merger that produced Alectra [EB-2016-0025 and EB-2016-0360]). The policy did require an earnings sharing mechanism in years six to ten of the deferral period, but only in the event, and to the extent, that utility profits exceeded a 3% deadband, a highly unlikely eventuality, given the typical returns in the Ontario electricity distribution sector.

In BOMA's view, there is clearly no need for such substantial incentives to encourage the two very large Ontario natural gas utilities to merge. It makes no sense, given that they are the only two significant gas utilities in Ontario, and have been highly profitable for decades, with their actual return much more often than not exceeding their allowed ROEs. The utilities have, in fact, already effectively merged. They have been under common ownership since EGD's acquisition of Spectra, the ultimate parent company of Union Gas Ltd., in March 2017. They are already working closely together on many issues, including the companies' 2018 Cap & Trade application. They are already working in tandem to provide essentially the same Cap & Trade submission. They could, if they so choose, continue to operate their separate networks, with a common platform for common costs. They plan, in any event, to maintain separate rate zones. It is not clear to what extent their capital allocation and planning processes will be totally integrated, and whether and when a single Distribution System Plan will be in place. EGD and Union are merging under section 43 because it offers then the opportunity, in the event they can persuade the Board to apply the electricity merger policy to their transaction, to keep an enormous windfall. If the Board applies the electricity merger policy to this transaction, EGD would obtain a huge windfall, which it would not receive were the companies to operate as two separate utilities, and with common service being provided through a service company, or in some other options.

These are the only gas utilities in the province, both owned by the same company, Enbridge Inc. Both Union and EGD are each in their own right very large companies. There is no need to consolidate the industry from two companies to one. With two independent gas distributors in

the province, the Board at least had the opportunity to hold up the best practices of one utility to the other to seek improvements for ratepayers. That opportunity will no longer exist.

Second, there is not, and has never been, any explicit Government policy to merge EGD and Union into one company.

For all these reasons, it is important to fashion a merger policy appropriate for the gas industry, not to simply automatically apply the merger and rate policies that were developed exclusively for the electricity industry, including the "no-harm" test, and the ten year rebasing deferral period. These policies, crafted for a different industry and different Government policies, need to be adapted and modified before being applied in this case to the merger of two multi-billion dollar gas distributors. That is why the intervenors' Issues List starts with the issue of what should be the appropriate test for approval of the merger, how that test should be applied in this case in light of the Board's statutory objectives, in relation to natural gas, and have the applicants meet the appropriate test (Issues 1, 2, and 3), Government policies with respect to gas industry across the electricity industry, the ownership characteristics of the two industries, and the drivers of the particular merger, and finally in Issue 3, have the applicants meet the appropriate test.

The considerations discussed above are also the reason why the issue of whether a deferral of rebasing is an appropriate part of a merger policy for the province's two large natural gas utilities, which are already under common ownership.

In BOMA's view, it is critical for the Board to look with fresh eyes at whether the subsidies given to electrical utilities to incent them to merge are necessary or even desirable in the proposed merger, and what other requirements are required to protect ratepayers over any

deferral rebasing period, if one is required, such as revised earning sharing arrangements (Issues 4 and 5).

Both EGD and Union have made commitments as to matters they will address in their future rates cases, including 2019 rates, including important cost allocation issues. The nature of the 2019 rate proceeding is an important issue (Issue 6).

Issue 7 deals with the impact of the merger on other Board policies, rules, or orders, for example, regulations of new storage. These matters are raised in Issue 7.

Issues 8, 9, 10, and 11 deal with conditions that the Board should consider attaching to any approval it may give to the merger, and how such condition would relate to the current undertakings; a subject which EGD discussed at some length in its Application.

It is important for everyone to remember that parties are not making final arguments at this time, but rather assisting the Board to determine an Issues List, which will allow all these important questions to be raised. Parties should have the opportunity to address the above issues, and the Issues List should contain issues dealing with what test should be applied and whether the Board should approve the merger, for what period, if any, should the merged gas utility be allowed to retain 100% of the savings realized through the merger, or any portion of the savings, and what the other elements of the ratemaking framework should be adopted subsequent to the merger.

BOMA's Comments on EGD's submission dated January 19, 2018

BOMA has several concerns with EGD's submission.

EGD stated at paragraph 8 of its submission that:

> *"The Rate Handbook for Utility Rate Applications (Rate Handbook) issued by the Board in October 2016 confirms that the Board's MAAD policies provide guidance for both gas and electric utilities."*

The Rate Handbook confirms no such thing. The Rate Handbook deals with, as its title implies, rates, not consolidations. It provides guidance to electricity distributors and transmitters, gas distributors, and Ontario Power Generators on what their rates applications must contain. The Rate Handbook applies to gas distributors rate submissions but not to gas companies' mergers. The Handbook is thirty pages long, with only about half a page dedicated to MAADs, which deal very briefly with gas rates filings following a merger.

EGD states, again that the OEB has also issued a Handbook to Electricity Distributors and Transformer Consolidation on January 19, 2018. However, that Handbook deals only with electricity mergers, not gas mergers. EGD also states, rather cryptically, at paragraph 9 of its submission that the Rate Handbook also "links" the Board's Filing Requirements for Natural Gas Rate Applications, although no specific reference to the Rate Handbook text is provided.

At paragraph 11 of its submission, after discussing the above "linkages", EGD concludes:

> *"It is evident from the Rate Handbook itself and from the "linkages" among the Consolidation Handbook, the Rate Handbook and the Board's MAADs policies provide guidance for consolidation by both gas and electricity distributors".*

Unfortunately, this statement is incorrect. Despite the alleged linkages, the Rate Handbook deals with both electricity and gas rates filings, and the Handbook to the Electricity Distributor and Transmitter Consolidation (which EGD refers to as the Consolidation Handbook) deals only with electricity.

The Rate Filing Requirements for Natural Gas Rate Application dated February 16, 2017 provides detailed guidelines for the filing of gas distributors' rate submissions. They contain an introduction of four pages, and a forty-one page chapter, entitled "Cost of Service Applications".

The only reference to MAADs applications contained in the forty-five page document is in a three-line sentence, that states:

> *"In the first cost of service application following a consolidation, the applicant is expected to address any rate-making aspects of the MAADs transaction, including a rate harmonization plan and /or customer rate classifications post consolidation."*

The Rate Filing Requirements for Natural Gas Rate Applications are about rates, not gas company consolidations.

And, the Board's MAADs policies do not provide guidance to gas mergers. They explicitly, on their face, deal solely with electricity distributor consolidations. Put another way, EGD's conclusion in the above quotation does not flow from the claimed "linkages" in paragraphs 8 and 9 of its submission. The conclusion put forward in paragraph 11, quoted above, is a complete non-sequitur.

EGD attempts to buttress its erroneous conclusion, discussed just above, by citing the fact that the RRFE is now an RRF. BOMA agrees that the RRFE is now an RRF, but that does not mean that the Board's electricity merger policies now apply to gas utilities. Rather, it reflects the fact that the Rate Distributor Handbook now requires that both gas and electric distribution utilities must comply with the outcomes based approach to rate regulation, which it reviews in some detail.

Finally, by the same process of analysis, BOMA concludes that the applicant's statement at paragraph 7 of its submission, "that the Board's MAADs policy and associated rate policies are integrated, are intended to apply to gas utilities as well as electric utilities" is also wrong. While the Board's MAADs policy and its related electricity distribution rate policies are linked, and should generally be considered together, and one would expect that the Board's gas merger policy and gas ratemaking policy would be similarly linked (which is why the intervenors have added specific issues on the deferred rebasing policy), there is currently no MAADs policy for the merger of the province's two major gas utilities, nor any consideration of the appropriate rate treatment for the gas entity after the merger to ensure ratepayers are properly protected. That policy will, BOMA believes, be established by the Board in this proceeding. And that is why the intervenors believe issues relating to rebasing, and deferral of rebasing, should be part of the Issues List.

BOMA's Assessment of EGD's critique of the Intervenors' Issues List (paragraphs 24 to 42 of EGD's Submission

The first group of comments, paragraphs 24 to 33, deal with EGD's efforts to oppose adding to the Issues List the appropriate test for the merger of EGD and Union Gas, how that test should be applied, and have the applicants meet that test.

Most of what EGD did in these paragraphs was simply restated that the no-harm test was the test the Board has historically applied to proposed merger of electric distribution utilities over the last several years. BOMA does not dispute that the no-harm test, as first articulated in the Combined Proceeding, was applied in several subsequent electricity merger cases. However, in the Combined Proceeding, held many years before the Board created its current electricity merger

policy, there was no issue relating to deferral rebasing or joining of two businesses, and no incentive provided by Board policy. It was also a non-arm's length transaction. In the Combined Proceeding (EB-2005-0415, November 3, 2005), the opposition to the several acquisitions being proposed by three utilities were arguing that there should be a very wide test applied; namely, whether a better deal should have been obtained by the seller. The Board, understandably, had difficulty accepting that test for both fairness and practical reasons. This position is not taken by parties in this case. They simply want the ability to ask IRs and make submissions about other common sense ways of judging the transaction, and whether related ratemaking issues, such as the deferred rebasing are appropriate.

Moreover, the only gas case that EGD found was not a merger or consolidation case at all, but rather the sale in December 2009 by Union Gas of an 11.7 km long piece of pipe near Dawn to a joint venture to be formed and jointly owned by Union Gas' parent and DTE. The transaction was not done pursuant to section 43. The case (EB-2008-0411) was in no way analogous to the complicated merger transaction between already commonly owned parties that is the subject of this proceeding. It remains clear that the Board has not developed a merger policy for gas utilities in Ontario, nor has it been called upon to apply the MAADs electricity policy to a transaction like the one before us. Many other jurisdictions use other tests.

The decision of the one-person panel in the recent NRG/EPCOR case was dealing with a very small "tuck-in" acquisition by EPCOR of a very small gas utility, which, given the operational history that very small utility of NRG was obviously going to be of significant benefit to its ratepayers. But that panel appeared to apply the electricity's MAADs guidelines to that

transaction by default, and did not discuss the issue of what the appropriate test would be, in part because that issue was not raised in this case. The circumstances confronting the Board in that proceeding can be easily distinguished from this proceeding.

As for EGD's concern that it has filed evidence that addresses the no-harm test and it is not fair to change the rules, EGD took the chance when it complied its evidence that the no-harm test would necessarily apply. It will have ample opportunity to reply to any interrogatories on the issue of the appropriate test and related rate treatment, if necessary, file supplementary evidence. BOMA would not object if EGD were to request additional time, in the event it needed to file additional evidence, in light of adjustments to the Issues List.

Deferred Rebasing Period

EGD addressed this part of the intervenors' proposed Issues List at paragraphs 34 to 38 of its submission.

The cases cited by EGD are electricity cases and, as stated earlier, the Consolidated Handbook, the 2007 Report, and the 2015 Report, apply only to electricity mergers.

An important issue for this case should then be a different approach to the manner in which the MAADs electricity guidelines treated the ratemaking framework after a merger, including whether the deferral rebasing privilege accorded to electric utilities, is appropriate in the present cases.

As noted above, the two major utilities do not require incentives to merge. They are already a single economic unit, as their parent companies have merged. There is no underlying

Government policy that requires the merger application. EGD's evidence is that the transaction costs are not material. The integration costs are not particularly large, and mostly within the control of EGD, as a matter of good business practice. The failure of the electricity MAADs guidelines to ensure sharing the benefits of the merger with customers may have been justifiable in the electricity distribution context to create sufficient incentives for the electric utilities to consider merging in spite of the inclination if some municipal council owned companies not to do so, for fear of losing load benefits. That same argument cannot be easily applied to the present case. The argument that the customers will be better off because the merged entity will be under a price cap, rather than some other regime, is mostly artifice, especially in light of the fact that under the most recent iteration of the ACM/ICM policy, the parties to a merger are free to pursue ICM capital funds in any year(s) after the merger, and as the qualification for inclusion in an ICM has been continuously loosened in a series of decisions by the Board over the last ten years. For an example of what can happen, look to the large ICM proposals of Alectra for both its Enersource and PowerStream "rate zones" in the ongoing Alectra rates case (EB-2017-0024). If the proposals were to be approved by the Board, the lack of ratepayer protection would be apparent.

Finally, due to various commitments of both Union and EGD from the IRM period and investments to deal with various matters in the 2019 rates, or promptly after the end of the IRM, BOMA is of the view that the issue of whether there should be a near term rebasing at least requires examination in this case, and at least that more clarity is required in the scope of the 2019 rate application(s).

Enbridge Gas Distribution Inc.
and Union Gas Limited

Application for approval to amalgamate Enbridge Gas Distribution Inc. and Union Gas Limited

PROPOSED ISSUES LIST

[Bold & italicized numbers reference utilities' proposed issues list.]

TEST FOR APPROVAL OF THE MERGER

1. What is the appropriate test for approval of the merger under section 43(1)(c) of the Ontario Energy Board Act, 1998; "no harm", "net benefits", other?

2. How should the test for approval be applied in this case, including in consideration of the Board's statutory objectives in relation to gas? ***[Utilities Issues 1, 5, 6, 7 and 8]***

3. Have the applicants met the appropriate test?

REBASING DEFERRAL

4. Is deferral of rebasing appropriate in the context of this application?

5. If so:

   (a) What is the appropriate deferral period?

   (b) Is an earnings sharing mechanism [ESM] appropriate and if so what should that mechanism be and when should it apply? ***[Utilities Issues 3 & 4]***

   (c) What additional considerations and requirements are appropriate to protect the interests of customers pending rebasing?

6. What commitments to future action have the utilities made during their respective 2013-2018 rate plan terms, what other rate setting issues merit attention now (including cost allocation issues), and when and how are these commitments and issues to be addressed?

IMPACTS OF THE MERGER

7. Would the proposed merger impact any other OEB policies, rules or orders (e.g. regulation of new storage, Storage and Transmission Access Rule (STAR))? If so, what are those impacts and how should the Board address them?

8. If leave is granted, what conditions should be attached?

9. What is the status of the Undertakings to the Lieutenant Governor in Council of Ontario?

10. Should the undertakings be replaced by a condition of the approval of the OEB of the proposed merger?

11. If so, what should the content of the condition be?

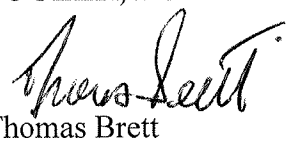
For all these reasons, the reasonable, common sense, and fair course of action to include the issues related to rebasing deferral on the issues list for this case, including whether there should be a deferral, and if so, the appropriate term, earnings sharing, and the terms and conditions under which it operates.

The issue with respect to the impact of the merger on various other Board orders and policies, in particular, in storage creation, allocation, and management, should be an issue on the list. The differential interests on existing ratepayers of Union and EGD need to be expressed. Union ratepayers may be worse off if EGD is able to use Union's storage for its own purposes. There is a limited number of such issues that should be examined. If three separate rate zones are to be retained, how will the allocations of costs and benefits be applied to the three and allocated?

For all these reasons, BOMA recommends the Board adopt the intervenors' Issues List (a copy is attached to this letter). It is fairer and does not assume the automatic transfer of MAADs electricity guidelines to the gas industry, and will be more helpful to the Board and parties.

Yours truly,

FOGLER, RUBINOFF LLP



Thomas Brett
TB/dd
cc: All Parties *(via email)*