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June 15, 2018

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli,

RE: EB-2017-0306/EB-2017-0307 – Enbridge Gas Distribution Inc. and Union Gas Limited Application for Amalgamation and Rate-Setting Mechanism – Submissions of LPMA

Please find attached the submissions of the London Property Management Association in the above noted proceeding.

Yours very truly,

Randy Aiken

Randy Aiken
Aiken & Associates

EB-2017-0306
EB-2017-0307

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 198, c. 15 (Sched. B);

AND IN THE MATTER OF an application by Enbridge Gas Distribution Inc. and Union Gas Limited, pursuant to section 43(1) of the *Ontario Energy Board Act, 1998*, for an order or orders granting leave to amalgamate as of January 1, 2019;

AND IN THE MATTER OF an Application by Enbridge Gas Distribution Inc. and Union Gas Limited, pursuant to section 36 of the *Ontario Energy Board Act, 1998*, for an order or orders approving a rate setting mechanism and associated parameters during the deferred rebasing period, effective January 1, 2019.

SUBMISSIONS OF LONDON PROPERTY MANAGEMENT ASSOCIATION

A. INTRODUCTION

Union Gas Limited ("Union") and Enbridge Gas Distribution Inc. ("Enbridge") jointly filed an application dated November 2, 2017 with the Ontario Energy Board ("OEB") under section 43(1) of the *Ontario Energy Board Act, 1998* ("OEB Act") for approval to effect the amalgamation of Union and Enbridge (jointly referred to as the applicants), into a single company referred to in the application as Amalco. Union and Enbridge prepared the merger application with guidance from the OEB's Handbook to Electricity Distributor and Transmitter Consolidations ("MAADs Handbook"). The OEB assigned the application the file number EB-2017-0306.

The applicants have been under common ownership since February 27, 2017 when Enbridge Inc. merged with Spectra Energy Corp.

On November 23, 2017, Union and Enbridge filed another joint application with the OEB under section 36 of the OEB Act for approval of a rate setting mechanism and associated parameters, effective January 1, 2019. The filing was done in accordance with the MAADs framework and the applicants have requested a price cap IR adjustment mechanism beginning in 2019 for a ten-year period. The OEB assigned the application the file number EB-2017-0307.

The OEB issued its Decision and Procedural Order No. 3, dated March 1, 2018 in which it determined that pursuant to section 9.1 of the *Statutory Powers Procedure Act* and section 21(5) of the OEB Act, it would combine the two applications as this would allow for a more efficient hearing and allow the OEB and parties to address the interdependencies between the applications.

The OEB issued the approved Issues List as Schedule A to the Decision and Procedural Order No. 3 noted above.

The following are the submissions of the London Property Management Association ("LPMA") on the issues identified by the OEB in the Issues List. As LPMA members are served primarily by Union, the submissions that follow are focused on the impacts to Union and its customers. In addition, LPMA is making a number of general submissions with respect to the joint applications.

B. GENERAL SUBMISSIONS

1. Applicability of the MAADs Handbook

The applicants have based their application almost entirely on the OEB's Handbook to Electricity Distributor and Transmitter Consolidations ("MAADs Handbook"). LPMA submits that the applicability of the MAADs Handbook to the merger of the two gas distributors has already been determined by the OEB.

In the Decision and Procedural Order No. 3 dated March 1, 2018, the OEB stated (page 4):

> *The primary issue before the OEB with respect to determining an Issues List is whether the OEB's electricity MAADs policy framework as discussed in the MAADs Handbook applies to this application. The MAADs policy framework was established to encourage and incentivize consolidation within the electricity distribution sector. There is no such policy driver in the gas distribution business. There is no reference to natural gas in the MAADs Handbook. The OEB will therefore not restrict the ability of OEB staff and intervenors to question the applicability of the policies within the electricity MAADs policy framework.*

The OEB further stated at page 6 that:

> *The OEB does not agree with the arguments of the applicants and accepts the position of intervenors and OEB staff that all aspects of the MAADs Handbook do not automatically apply to natural gas. The MAADs Handbook does not specifically reference natural gas and there is no specific guidance in the Handbook as to how gas mergers should proceed. The OEB is of the view that issues such as the deferral period and earnings sharing mechanism are legitimate areas of inquiry and are not pre-determined in this case. The OEB may find that the MAADs Handbook applies in part or in whole, but this does not preclude parties from arguing for or against the applicability of specific elements of the MAADs Handbook, with the exception of the applicability of the no harm test.*

LPMA submits it is clear that the MAADs Handbook and the associated policy is not applicable to the proposed merger of Union and Enbridge in its entirety. The MAADs policy framework was developed to encourage and incentivize consolidation within the electricity distribution sector in Ontario which has many more distributors than does the natural gas industry. There is no policy to encourage gas distributors in the province to merge. In fact, the opposite is true. The OEB has encouraged new parties to enter the natural gas industry in Ontario through its policy to require competition to serve previously unserved areas in the province.

LPMA submits that the OEB should judge the application on its own merits and the potential impacts on natural gas ratepayers.

2. High Level Cost Estimates

All of the evidence of potential cost savings provided by the applicants in this proceeding is based on high-level estimates based on a "high-level business plan, a high-level plan" (Tr. Vol. 1, page 40). The applicants further indicated that they have not done any detailed planning (Tr. Vol. 1, page 43):

> *MR. SHEPHERD: You have a plan for how to save money if you amalgamate, right? That's the one you presented to the Board.*
> *MR. KITCHEN: We have a high-level plan, yes.*
> *MR. SHEPHERD: Have you gone through that plan and said, which of these things can we do now?*
> *[Witness panel confers]*
> *MR. KITCHEN: No, and I go back to my answer I've already given, that we haven't done detailed planning, and we will commence that once we have the Board's decision.*

LPMA submits that the OEB should ignore the forecasted savings projected by the applicants. No detailed planning has taken place and all of the high-level estimates provided in this proceeding are nothing but pie-in-the-sky figures that have absolutely no evidence to back them up.

The reduction in rates to ratepayers of Amalco as compared to the stand alone separate entities fails to take into account shared savings that are expected to be in place by the end of the year as the result of the merger of the parent companies through the shared service harmonization plan (Tr. Vol. 1, page 50). The hypothetical stand alone rates scenario is based on a no sharing of staff and no rationalization of activities (Tr. Vol. 1, page 146). In plain words, the stand alone scenario does not reflect the changes that are already going on and the changes that will take place in the future.

The Union witness even indicated that their assumptions and forecasts used for the stand-alone option are not what the OEB would see if Union were to file a five-year Custom IR plan if the proposed amalgamation did not proceed (Tr. Vol. 1, page 17):

> *MR. SHEPHERD: Why would it take you all of this year to file the -- to prepare for the application? You've got all the numbers, right? You provided them to the Board.*
> *MR. KITCHEN: Mr. Shepherd, if we were filing a five-year custom IR we would have to update our forecast, obviously, and make an application on that basis. We're not in the position to file a custom IR for either company at this point.*

This highlights the complications associated with comparing one hypothetical situation to another hypothetical situation. The difference is completely driven by unsubstantiated assumptions and high-level estimates that are not supported by any detailed planning.

LPMA likens the situation in this proceeding to a person buying a single detached house and planning to add onto the back and add a rental unit in the basement. High-level cost estimates for the addition and the rental conversion are obtained and can be added to the expected purchase cost of the house to determine if the economics support the project.

The person buys the house without a home inspection and finds that the roof needs to be replaced, the wiring is out of date and needs to be replaced to come up to code and the gas furnace is on its last legs. Furthermore, upon approach the local municipality they discover they cannot build the addition because it violates the setback requirements from the property line of the municipality and basement rental units are not allowed in the neighbourhood.

The high-level estimates are now meaningless because no detailed planning (home inspection, building permits, etc.) was undertaken before the house was purchased. LPMA submits that the OEB should not accept the proposal of the applicants based on their projected savings or rates impacts on customers because no detailed planning is available to support any of their guesses.

3. Failure of the Current IR Plans to Provide Rebasing Benefits to Ratepayers

The applicant's proposal has a major flaw in it. It assumes no rebasing of rates for 2019 even though rebasing is a key component of an IR plan. As submitted in more detail under MAADs Application Issue #3 below, it is the OEB's view that a thorough cost-of-service rebasing must occur at the end of each IR plan's term before a new plan is put in place. The applicants current IR plans end on December 31, 2018 and the new plan takes effect January 1, 2019. However, no cost-of-service rebasing is planned until 2029.

Moreover, the OEB also has indicated that rebasing is an important ratepayer protection feature of an IR plan and that through robust rebasing, efficiency improvements will be revealed and the benefits passed on to ratepayers through base rates for the next year. The current proposal has eliminated this ratepayer protection feature and withholds the benefits of efficiency improvements from IR plans that expire at the end of this year.

Elsewhere in this submission, LPMA submits that base rate adjustments are required to 2019 rates to reflect this omission from the current proposal.

4. Merger May Not Proceed Based on OEB Decision

The applicants have indicated that final approval for the merger will not come from the relevant Board of Directors until after they review the OEB's decision in this proceeding and implied that if they were directed by the OEN to rebase or start earnings sharing in the first year, that the amalgamation would not proceed (Tr. Vol. 1, pages 12-14).

LPMA submits that the OEB should not let this implied threat to influence their decision on any of the issues in this proceeding. If the applicants ultimately decide to not amalgamate, that is just fine with LPMA.

Given the lack of any detailed planning, the use of questionable hypothetical rate scenarios, no rebasing benefits at the end of the current IR plans, no productivity/stretch factor included in rates, no earnings sharing to provide ratepayer protection over the entire deferred rebasing period and other deficient areas of the applicant's proposal,

LPMA submits that it is likely safer from the ratepayer's point of view that the merger not proceed at this time.

This would not preclude the merger at a future point in time, once a rebasing has taken place, cost have been allocated and rates designed based on current costs - not costs that are significantly out of date – and a detailed amalgamation plan and study being completed – a plan that can be fully reviewed and tested by the OEB and intervenors, unlike the pie-in-the-sky approach taken in this proceeding.

LPMA also notes that Union ratepayers would likely be better off, and no worse off, on a stand-alone basis than they are today. This is because there are expected cost reductions through the shared services harmonization plan currently underway by the parent company which is expected to be completed by the end of this year (Tr. Vol. 1, pages 50-51).

As a result, LPMA submits that the decision to not amalgamate would meet the requirements of the no harm test as ratepayers would be better off and at least no worse off than under the current situation.

5. Rate Plan Application Should be Denied

It is the submission of LPMA that the OEB should approve the amalgamation of Union and Enbridge, given that they are already under common ownership. However, it is also the submission of LPMA that the OEB should not approve the rate plan as proposed.

It is the submission of LPMA that the no harm test is met in the absence of the rate plan proposal. The proposed rate plan, however, harms ratepayers or has the potential to harm ratepayers and should be denied or modified significantly, as proposed throughout this submission to ensure that ratepayers are not worse off than under the scenario of no amalgamation.

LPMA submits that the rate plan application should be denied by the OEB for a number of reasons. The following is a brief listing of each of these reasons. Each topic is discussed in further detail in this submission.

First, the proposed price cap methodology includes no productivity or stretch factor. This eliminates any benefit to ratepayers in sharing of expected cost reductions over the entire deferred rebasing period. Inclusion of such a factor would provide benefits to ratepayers and added incentives to the utilities to find synergies and efficiencies.

Second, the proposed earnings sharing mechanism is a joke – a bad joke as far as ratepayers are concerned. It allows the shareholder to retain all over earnings over the first five years and all over earnings up to 300 basis points in years six through ten and 50% of anything over that level. The evidence in this proceeding indicates that the shareholder is happy to over earn by 20 basis points. An earnings sharing mechanism that rewards both the shareholder and ratepayers is needed, not a one-sided mechanism that overcompensates the shareholder.

Third, the MAADs policy does not apply. As noted above, there is no provincial or OEB policy to encourage the merger of gas distributors.

Fourth, no base rate adjustments have been made to reflect the efficiencies achieved over the 2014 to 2018 period. The OEB has indicated that rebasing is an important ratepayer protection feature of an IR plan and that through robust rebasing, efficiency improvements will be revealed and the benefits passed on to ratepayers through base rates for the next year.

LPMA notes that the applicants have repeatedly indicated in this proceeding that customers will benefit from synergies and efficiencies achieved throughout the deferred rebasing period at the end of the ten-year period when it rebases. They said the same thing at the beginning of the current IR plans and now there is no rebasing proposed to take place. How can ratepayers, or the OEB, take their word this time around?

Fifth, the distributors have continued to over earn and, in some years, over earn significantly on a normalized basis. This indicates that there have been significant changes in the costs and/or the cost structure of the distributors. For example, Enbridge has significantly reduced its workforce by 266 people since 2014, at an annual reduction in costs of $25 million (Tr. Vol. 1, pages 132-133). While this reduction in costs may be partially offset by increases related to capital additions, there is no guarantee that the allocation of these two different types of costs is neutral by rate class. This bring into question whether the rates can be just and reasonable for all rate classes in the absence of a comprehensive cost allocation study that reflects the change in cost structures that have taken place since 2013.

6. The Path Forward if Rate Plan is Denied

LPMA submits that the OEB should direct Union and Enbridge to file a full cost of service application, including a comprehensive cost allocation study, either individually or as a joint entity. LPMA further submits that the application(s) should be filed with a test year no later than 2021.

If the rate plan as proposed is denied by the OEB, it is not clear whether the applicants would continue with the amalgamation. They may decide not to amalgamate, or they may defer the timing of the merger. Regardless of the outcome, LPMA submits that a cost of service rebasing application is required as soon as possible.

LPMA realizes that a cost of service application is not possible for 2019 rates and may not be possible for 2020 rates, given the time it takes to put together the application and evidence and the time to review it through the regulatory process. As a result LPMA believes that a cost of service filing for 2021 is more practical.

In the meantime, rates for 2019 and 2020 will have to be set. LPMA submits that the Union IR plan should continue for Union over this period based on its existing plan terms. These terms would include the existing capital pass-through mechanism, earnings sharing mechanism and an escalation factor of 40% of inflation, and a Z factor materiality threshold of $4 million. The tax refund adjustment of $17.4 million proposed by Union in this proceeding would be dealt with in the application for 2019 rates.

Enbridge should also continue with its current Custom IR plan, unless it wishes to switch to the current Union price cap IRM model using the same plan parameters as used by Union. The base rate adjustments proposed by Enbridge would be dealt with in the application for 2019 rates.

As part of the required rebasing no later than for 2021 rates, the OEB should direct the distributors (or distributor) to include a utility system plan that demonstrates the management of the overall system, whether as an amalgamated entity or as separate entities under common ownership. The plan should be detailed and comprehensive and show how it maximizes the benefits for ratepayers.

C. SUBMISSIONS ON ISSUES

MAADs APPLICATION ISSUES LIST

“NO HARM” TEST

1. Have the applicants appropriately applied the ‘No Harm” test in this case, including in consideration of the OEB’s statutory objectives in relation to natural gas?

LPMA submits that the applicants have not appropriately applied the no harm test in this case. The applicants have relied entirely on fictional savings calculated between their

rate proposal for Amalco and stand-alone rates assuming the applicants do not amalgamate and the promise of benefits to ratepayers at the end of the ten-year deferral period when rebasing would take place.

As noted elsewhere in this submission, the estimates of the savings to ratepayers over the deferral period are based solely on high-level estimates that have not been supported by any detailed planning because this planning has not taken place. The stand-alone scenario used as the base to calculate the supposed ratepayer benefits are devoid of any reductions associated with the shared service harmonization plan that is scheduled to be completed by the end of year, as noted earlier in this submission. The hypothetical stand alone scenario assumes no sharing of staff and no rationalization of activities.

The applicants have not provided a detailed plan for the amalgamation and the resulting cost reductions. Indeed, the evidence in this proceeding was focused on how much the costs would have to be reduced in order to finance the transaction costs, cover the supposed reduction in revenue collected from ratepayers and provide the shareholder of Amalco with a return on equity in excess of the approved level. When pressed to explain how these cost reductions would be achieved, the applicants were only able to provide high-level estimates that were not supported by any detailed review or planning. In fact, the applicants indicated that the detailed planning would not commence until the OEB approved the amalgamation.

The applicants have stated that benefits from the amalgamation would be shared with ratepayers upon rebasing at the end of the ten-year deferral period. However, LPMA submits that this is a hollow promise. First, there is no guarantee that rebasing would take place. There is no rebasing planned for the end of the current IR plans that are only five years in length. Why should ratepayers blindly accept the word of the applicants for something that may or may not happen at the end of a ten-year IR plan?

Second, there is no guarantee of savings to be shared with ratepayers. As noted above, there has been no detailed planning undertaken with respect to how the cost structures will be changed.

The applicants have also not provided any evidence on what it expects the overall cost structure to be following the deferral period and to explain the impact on Union and Enbridge customers. The applicants have only stated that, based on the high-level cost savings projected for the ten-year deferral period the cost structure to service the Union and Enbridge distribution areas, the cost structure will be lower following the deferred rebasing period in comparison to the status quo. No evidence has been provided to support this.

LPMA submits that in reviewing the proposed transaction, the OEB should examine the long-term effect of the consolidation on customers.

LPMA submits that it would have been reasonable to see a forecast of costs to service the Union and Enbridge distribution areas following the ten-year deferral period. This is consistent with the EB-2016-0276 Decision and Order dated April 12, 2018 in which Hydro One Inc. requested approval to purchase Orillia Power Distribution Corporation.

In that Decision, the OEB stated (page 13):

> *The OEB is of the view that it would have been reasonable to see a forecast of costs to service Orillia customers beyond the ten year period and an explanation of the general methodology of how costs would be allocated to Orillia ratepayers after the deferral period. Hydro One takes the position that this information is not known. The OEB recognizes that any forecast of cost structures and cost allocation 10 years out would include various assumptions and could not be expected to be 100% accurate. However, the OEB has highlighted its concern and its need to better understand the implications of how Orillia customers will be impacted by the consolidation beyond the ten year period. In the absence of information to address that OEB concern, the OEB cannot reach the conclusion that there will be no harm.*

LPMA submits that the OEB should not consider temporary rate impacts proposed by applicants, and other such temporary provisions, over a deferred rebasing period to be demonstrative of no harm as they are not supported by, or reflective of the underlying cost structures of the parties involved. These temporary rate impacts may not be sustainable or beneficial to ratepayers in the long term.

In summary LPMA submits that based on the lack of any evidence related to cost structures and cost allocation ten years out at the time of the proposed rebasing, the OEB should come to the same conclusion that it did in the Hydro One/Orillia decision. Simply put, the OEB cannot reach the conclusion that there will be no harm.

2. Have the applicants met the test?

LPMA submits that the applicants have not met the no harm test.

As noted above, there is no detailed plan or forecast for the cost structure or cost allocation beyond the deferred rebasing period. As a result, the OEB cannot conclude that there is no harm to ratepayers in the long term.

The applicants cannot guarantee that there will be a cost of service rebasing application following the deferral period. Nor can they guarantee that there will be any cost savings to accrue to ratepayers at that time assuming a rebasing actually takes place.

The lack of a comprehensive cost allocation study that is based on current up to date information that reflects the significant changes that have taken place since the 2013 study was done (using 2011 actual data) means that some customers are likely being harmed through higher rates than they would otherwise be required to pay. Examples of the significant changes that have taken place since 2013 include the massive investments in the Dawn to Parkway system and the Panhandle Reinforcement on the Union system, and the elimination of more than 260 full time equivalent workers for Enbridge.

LPMA also submits that by not rebasing at the end of the current IR plans, ratepayers are being harmed by the fact that they are not receiving any benefits of the efficiencies that the distributors have gained over the 2014 through 2018 period, even though both distributors over earned on a normalized basis to a great extent in each and every one of these years. As indicated in General Submissions Issue #3 above, the OEB has indicated that rebasing is an important ratepayer protection feature of an IR plan and that through robust rebasing, efficiency improvements will be revealed and the benefits passed on to ratepayers through base rates for the next year. Ratepayers are being harmed by the removal of this protection in the current proposal.

These efficiencies are significant and are reflected in the average over earning over this period of $23.0 million by Enbridge and $11.3 million by Union. These figures are calculated and discussed in more detail in Rate-Setting Mechanism Issue #1c.

LPMA notes that if these amounts were combined ($34.3 million) and used as a base rate adjustment to reflect the efficiencies gained in 2014 to 2018 in 2019 rates, then over the ten-year deferral period, these savings to ratepayers would total $343 million, nearly equalling the hypothetical savings calculated the applicants of just over $400 million.

There are also specific measures or changes that specifically harm or could harm Union ratepayers. Union is the smaller of the two distributors in this proposed amalgamation and LPMA submits that the potential impact on its ratepayers needs to be considered in determining if the nor harm test has been met.

Union currently has a Z factor materiality threshold of $4 million. The Amalco proposal is $1 million. This means that Union ratepayers would be exposed to recovery of an incremental amount of up to $3 million per Z factor event. Clearly this results in harm to Union ratepayers.

In the long term, LPMA is concerned with two potential changes beyond the ten-year rebasing period that would be detrimental to Union ratepayers. These changes include rate harmonization and the treatment of excess storage.

The applicants have indicated that they have not developed a plan to harmonize rates as part of this application but their understanding is that as per the OEB's handbook for consolidations, a consolidated entity is expected to propose rate structures and rate harmonization plans following consolidation at the time it files its rebasing application (Exhibit C.LPMA.42). Those plans would be reviewed by the OEB at the time of rate rebasing of the consolidated entity.

LPMA submits that the harmonization of rates would likely result in significant increases for most of its members. The vast majority of LPMA members are M1 customers (residential or commercial). As Attachment 1 to Exhibit C.LPMA.42 shows, the delivery charges for these customers are significantly lower than the charges for Enbridge customers. In particular, Union M1 residential customers pay nearly $60 less a year, or more than 10% less than Enbridge residential customers. Similarly, Union M1 commercial customers pay about $1,000 less, or more than 30% less than similar Enbridge customers in delivery charges. This reflects a significant potential for harm to not only to the majority of LPMA members but also to all residential and small commercial customers served by Union. Clearly rate harmonization has the potential to cause harm to these customers.

In the NGEIR Decision (EB-2005-0551), the OEB required Union to reserve 100 PJ of space at cost-based rates for in-franchise customers. This capacity met the needs of Union South and Union North customers at the time of NGEIR plus an allowance for further capacity needed to service the needs of Union at cost-based rates. The OEB also determined that Union would the flexibility to market the excess utility storage – the difference between the 100 PJ and the capacity required to serve in-franchise demands in any year – with the entire margin on storage transactions that are underpinned by this utility storage space accruing to Union's ratepayers, less an incentive payment to Union.

In this proceeding, the applicants have indicated that in their view, the amalgamation does not impact the NGEIR decision, and the margins provided by this excess storage, less and incentive to the utility, should continue to accrue to the ratepayers in Union South and Union North (Exhibit JT2.12). LPMA agrees with this position.

LPMA is aware that other parties may propose that the excess storage space should be provided to Enbridge customers at cost. LPMA opposes any such change related to the excess storage. As indicated in Exhibit JT2.12, Union South and Union North customers

receive a net benefit in rates of $4.5 million a year associated with this excess capacity. There is also a variance account to true up any variance between the actual net benefit obtained in any and the net benefit included in rates.

Any change in the treatment of this excess utility storage space and the net revenues generated from it, would result in harm to Union ratepayers. In particular, the current net benefit currently in rates would be lost, as would the true-up around this amount. Over a ten-year period, this could result in a loss to Union ratepayers of $45 million. In addition, if Union South and Union North require more storage capacity in the future, it would have to obtain that capacity at market-based rates, rather than use the cost-based storage that was specifically set aside for their future use in the NGEIR decision. This would result in additional costs to Union ratepayers. Clearly the no harm test would not be met with respect to this excess capacity.

LPMA submits that it is clear that a key consideration that the OEB must take into consideration is the underlying cost structure and the rate implications of that cost structure in both the short-term and in the long-term. LPMA further submits that the amalgamation is likely to result in some savings on account of eliminating duplication. However, that does not necessarily mean that the overall cost structure of Amalco will not be higher than Union's underlying cost structure that would exist in the absence of the amalgamation. The impacts of cost allocation, harmonization and excess storage capacity benefits are just some of the potential negative impacts on Union ratepayers.

In summary, LPMA submits that the applicants have not provided adequate evidence to support a finding that the no harm test has been met. LPMA further submits that if the applicants want to proceed with the amalgamation, they should provide a detailed plan that shows the cost structure, not only during the deferral period, but also after the deferral period, along with plans, if any, to harmonize rates, cost allocation methodologies etc., to show the impact on all customer classes. Only then can the OEB determine if the no hard test has been met.

REBASING DEFERRAL

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

LPMA submits that any rebasing deferral, regardless of how long the proposed deferral period is, is only appropriate if sufficient safeguards are put in place for ratepayers. The Union/Enbridge proposal do not contain sufficient safeguards in the view of LPMA.

First, LPMA submits that the required safeguards include, at a minimum, an earnings sharing mechanism that is fair and begins in the first year of the deferral period. This earnings sharing mechanism is discussed in more detail under Rate-Setting Mechanism Issue #1f below.

Second, it is submitted that an appropriate stretch factor needs to be in place for each of the deferred rebasing years. This ensures that ratepayers get to share in the savings associated with the amalgamation up front, rather than wait for ten years (in this proposal) for what amounts to non-guaranteed and probably imaginary savings that would come from a rebasing that cannot be guaranteed to occur. More details on the stretch factor proposal are provided under Rate-Setting Mechanism Issue #1c below.

Third, LPMA submits that base rate adjustments need to be made for the 2019 rates. These rate adjustments are in addition to those proposed by Union and Enbridge and would be reflective of the promises made by Union and Enbridge, and implicitly agreed to by the OEB in each of the current IR mechanism regimes currently in place for these distributors.

As part of the March 30, 2015 report entitled "Natural Gas Regulation in Ontario: A Renewed Policy Framework, Report on the Ontario Energy Natural Gas Forum" ("NGF Report"), the OEB stated that an acceptable ratemaking framework must, among other things, establish incentives for sustainable efficiency improvements that benefit customers and shareholders (page 18).

The NGF Report noted than an IR framework would provide utilities the opportunity to generate efficiencies during the term of the plan, with an up-front sharing of these efficiencies through a productivity factor. In Union's EB-2013-0202 approved IR plan for the 2014 through 2018 period, Union agreed to a productivity factor equal to 60% of the inflation rate and also reduced rates to a reflect a $4.5 million upfront productivity commitment.

The NGF Report also indicated that rebasing at the end of the IR term would ensure sustainable efficiencies were built into the new base rates on which another IR framework would be built. This was emphasized in a number of places in the NGF Report (with emphasis added):

> *The Board's view is that a thorough cost-of-service rebasing must occur at the end of each IR plan's term before a new plan is put in place. Rebasing is an important consumer protection feature. Through robust rebasing, efficiency improvements will be revealed and the benefits passed on to customers through base rates for the next period. (page 3)*

> *Rebasing at the end of the plan's term is another mechanism for ensuring that benefits flow to ratepayers. (page 16)*
>
> *The challenge is to ensure that the efficiencies do not result just in short-term shareholder benefits, but rather sustainable improvements that benefit ratepayers through lower utility costs and lower rates. A properly designed ratemaking framework will provide incentives for utilities to find cost efficiencies, and thereby to increase their earnings over the course of the plan. A properly designed plan will also ensure that customers benefit from efficiency gains both during the plan's period, through an appropriate adjustment or earnings sharing mechanism, and upon rebasing for the next plan period. The Board recognizes the importance of ensuring that customers achieve benefits from the beginning of the plan's term. (page 19)*
>
> *Each IR plan must begin with a robust set of cost-based rates, based on a thorough and transparent review. The Board's view is that a thorough cost-of-service rebasing must occur at the end of each IR plan's term before a new plan is put in place. Rebasing is an important consumer protection feature. Through robust rebasing, efficiency improvements will be revealed and their benefits passed on to customers through base rates for the next period. (page 25)*
>
> *As described above, the benefits of efficiencies can be shared with customers in two ways – during the term of the plan, through the adjustment mechanism, and in the base rates for the subsequent plan. With robust rebasing, all of the efficiency improvements achieved during the term of a plan would be built into the base rates for the subsequent plan. In this way, shareholders retain the benefits of any efficiency gains (that is, any achieved over and above the productivity factor) during the term of the initial plan, and all of the benefits flow to customers during the term of subsequent plans. (page 26)*

LPMA submits that the OEB should continue to follow the guidance set out in the NGF Report with respect to the need for the benefits that accrue to the utilities over the course of the IR mechanism period flow to customers during the term of subsequent plans. The current proposal of Union and Enbridge does not do this.

Unlike the mechanisms and situations discussed in the MAADs application handbook for electricity distributors, the terms for the IR plans of both Union and Enbridge will end on December 31, 2018. The next day a new IR plan is proposed to be implemented. There is no rebasing taking place at the end of the current IR plans. As a result, the efficiencies gained by the distributors, over and above what was built into rates through the productivity factor and the $4.5 million upfront productivity commitment from Union are not being reflected in rates during the subsequent IR plan being proposed to begin in 2019. In other words, no benefits will flow to ratepayers at the end of the current plans. This is in direct violation of the OEB's findings in the NGF Report.

The next question that has to be asked, is how large are these apparent efficiencies that are being kept from ratepayers? The answer is that they are quite large.

As is illustrated under Rate-Setting Mechanism Issue #1c, the average normalized over earning of Enbridge is $23.0 million for the 2014 through 2017 period. The average normalized over earning for Union over the same period is $11.3 million. Unlike the Enbridge over earnings figures which fall in 2015 and 2016 before rising in 2017 from the previous years, the Union figures show a distinct trend. The normalized over earnings for Union have increased each year and in 2017 are nearly three times higher than they were in 2014.

LPMA submits that the OEB should direct base rate reduction adjustments of $23.0 million for Enbridge and $11.3 million for Union. In the absence of rebasing, it is only through these base rate adjustments that ratepayers can receive the benefits that the OEB has indicated should be passed through to them at the end of an IR plan term and before the beginning of the next IR plan term. The Union/Enbridge proposal omits this significant benefit to ratepayers and results in neither just nor reasonable rates and is not aligned with the intent of the OEB's direction in the NGF Report or with the intent of incentive regulation where ratepayers benefit from the efficiencies achieved during an IR plan term.

In addition to the above noted base rate adjustments, LPMA submits that there should be a reduction in base rates associated with the Parkway Delivery Obligation ("PDO"). LPMA has had the opportunity to see the draft submissions of the Federation of Rental-housing Providers of Ontario ("FRPO") with respect to a base rate adjustment associated with the ("PDO") and supports those submissions.

At the very least, LPMA submits that the OEB should require Union (or Amalco) to file sufficient information to determine the appropriate PDO related costs and the allocation of those costs to the various rate classes beginning in 2019. This is another example of where there may have been significant changes since the last rebasing application that warrant a review of the determination of the associated PDO costs and the allocation of those costs to rate classes.

4. If so:
(a) What is the appropriate deferral period?

LPMA submits that a ten-year deferral period before rebasing, as proposed by the applicants can only be considered to be appropriate if there is adequate ratepayer protection built into the entire deferral period. This protection includes an earnings

sharing mechanism as described under Rate-Setting Mechanism Issue #1f below. The required protection also includes a stretch factor, as discussed under Rate-Setting Mechanism issue #1c below. Finally, the protection needs to ensure that ratepayers benefit upfront from the efficiencies gained by the distributors that have resulted from their current IR plans, as described under the MAADs Application Issue #3 above.

In the absence of these needed ratepayer protection measures, LPMA submits that a maximum deferral period of 5 years is appropriate. This was discussed in more detail under the General Submissions in Part B above.

(b) Is an earnings sharing mechanism (ESM) appropriate and if so, what should that mechanism be and when should it apply?

LPMA submits that an earnings sharing mechanism is not only appropriate, but is an essential element to provide both ratepayer protection and the sharing of efficiencies throughout any deferred rebasing period.

The specific proposals of LPMA with respect to the appropriate ESM have been provided under Rate-Setting Mechanism Issue #1f below.

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

As noted elsewhere throughout this submission, LPMA believes that the interests of customers are protected through four key areas. Each of these is discussed in greater detail under Rate-Setting Mechanism Issue #1 below.

First, an appropriate stretch factor throughout the deferred rebasing period is required to ensure that ratepayers share in savings through any deferred rebasing period and provide and added incentive to Amalco to find additional efficiencies.

Second, an asymmetrical earnings sharing mechanism is required that provides a deadband of 20 basis points required by the shareholder with 50/50 sharing above that level to reflect potential savings and efficiencies beyond that built into rates through the inclusion of a stretch factor.

Third, appropriate base level adjustments that provide benefits to ratepayers from the efficiencies achieved in the current IR plans for both distributors which was to flow to customers through rebasing for 2019 rates is required.

Finally, LPMA submits that there should be limits on the availability of the use of the incremental capital module ("ICM") during a deferred rebasing period. For example, if Amalco is over earning, the amount of rate increases related to the request for an ICM should be reduced to reflect this.

5. 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?

LPMA submits that Amalco should be free to bring forward responses to any of the commitments that have been made during their respective 2013-2018 rate plan terms during any deferred rebasing period for review by intervenors and the OEB. The application of any changes resulting from those responses may or may not be made during the deferred rebasing period. This would be determined by the OEB as part of its review of the responses to the commitments made.

LPMA believes that cost allocation issues deserve special mention. Amalco has stated that it intends to address the cost allocation of the Panhandle System and St. Clair System in its 2019 rates application (Exhibit B, Tab 1, page 31).

As the OEB is aware, cost allocation is a zero-sum exercise. Changes to the allocation of costs in one area results in cost decreases to some customers and cost increases to other customers. Without a full and comprehensive cost allocation study, those customers faced with the increase in costs associated with the narrow cost allocation review while being denied offsetting decreases driven by other changes. This would not and could not result in just and reasonable rates.

LPMA further notes that changes in cost allocation may not necessarily result in changes in rates during a deferred rebasing period. As an example, a rate class that is allocated less costs may already have a revenue-to-cost ratio that is less than 100%. In such a situation, the ratio may improve, but still be less than 100%. In this situation no reduction in rate would be appropriate, even though the allocated costs may have declined. Similarly, a rate class that is allocated more costs may have a revenue-to-cost ratio in excess of 100% and an increase in rates may not be justified.

LPMA notes that a comprehensive cost allocation study is almost always associated with a full cost of service rebasing application. However, it should be noted that a comprehensive cost allocation study can be completed based on an actual historical year rather than a forecast test year. Such a study is not as relevant as one done on a forward

test year but is still significantly better than a partial cost allocation study. The OEB may want to consider directing Amalco that if it brings forward any proposed cost allocation changes for consideration during the deferred rebasing period, the proposal must be based on a comprehensive, all encompassing cost allocation study based on the last year of historical data available. Any changes to that study from know or projected changes from the historical year should be identified, quantified and reviewed as part of the proposal.

Rate design changes are another area where a comprehensive review is required if any changes are proposed. Amalco has indicated that during the deferred rebasing period if may seek OEB approval to increase the percentage of its revenues recovered through fixed monthly charges (Tr. Vol. 6, pages 14-15). LPMA submits that in such a situation, Amalco would be reducing its forecast risk with respect to both weather variance and average use variance. Such a change would demand a review of the reduction in risks to the utility with respect to its return on equity.

In summary, LPMA submits that the OEB needs to closely monitor any proposed changes during the deferred rebasing period and keep in mind the intricate relationships within an issue and between different issues.

IMPACTS OF THE MERGER

6. 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 OEB address them?

LPMA submits that the OEB should continue to monitor all of its policies, rules and orders for any impact associated with the proposed merger. It is not likely that all potential impacts can be identified prior to the merger.

LPMA submits that the OEB should have a consultative process on an annual or bi-annual basis where any impacts of the merger on OEB policies, rules or orders can be discussed by all customer types (in-franchise, ex-franchise, system gas, direct purchase, wholesale, competing gas distributors, etc.). This forum would provide input into any potential changes or updates required in the OEB policies, rules or orders.

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

If leave is granted, LPMA submits that any attached conditions should be limited. LPMA is concerned that conditions may lead to increased costs and/or a reduction in potential

savings. This ultimately ends up costing ratepayers more and reduces their benefits from the merger.

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

LPMA makes no submissions on this issue.

9. To the extent that the Undertakings are impacted by this application, should any of the provisions of the Undertakings be replaced by a condition of any OEB approval?

As noted above, LPMA is concerned that any conditions of approval may lead to higher costs and/or lower potential savings. Any such conditions that result in a second best solution that results in higher costs or lower savings should be avoided if possible.

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

LPMA submits that the content of any condition imposed should be quantified in terms of additional costs or lost savings or efficiencies by Amalco. The treatment of these costs or lost savings should then be reviewed to determine whether they should be to the account of ratepayers or the shareholder, as a transaction cost associated with the merger.

RATE-SETTING MECHANISM ISSUES LIST

RATE FRAMEWORK:

The following submissions are based on the assumption that the OEB grants the applicant's request for amalgamation and a deferral period of more than five years in length.

It is the submission of LPMA that in this scenario, the no harm test can only be met through a price cap mechanism that provides adequate and immediate protection to ratepayers to offset the known and unknown longer-term impacts of the applicants' proposal which were discussed above under Issue #2 of the MAADs Application Issues List. These longer-term impacts are difficult, if not impossible, to predict and quantify and there is no guarantee that ratepayers will see any of these supposed long term benefits. This increases the level of risks faced by ratepayers in the longer term nd must be offset by benefits in the shorter term.

In other words, the following submissions are the minimum conditions under which the no harm test could be considered to have been met through up front benefits to customers to offset the longer-term consequences of the proposal.

<u>1. If the OEB grants the Applicants' request for approval of the amalgamation and deferral of rebasing, what should be the features of a Price Cap IR mechanism during the deferral period, including?</u>

<u>a. What is the appropriate inflation factor [I]?</u>

The applicants propose to use the quarterly Gross Domestic Project Implicit Price Index Final Domestic Demand ("GDPIPIFDD") Canada index from Statistics Canada as the inflation factor. The inflation factor would be calculated annually following the release of the second quarter data by Statistics Canada which usually occurs in August of each year. The annual calculation would be the average of the four quarters ending in June of each year. This is the same methodology that Union has used in its previous price cap formulas.

LPMA submits that the OEB should approve the continuation of the one-factor inflation factor using the GDPIPIFDD and the calculation methodology proposed by the applicants.

LPMA is aware that the OEB uses a two-factor inflation factor for the electricity distributors and some parties may propose that it also be used for Amalco. The second factor used in the electricity price cap is the increase in average wages.

LPMA does not support the use of the two-factor inflation factor. A review of the two-factor approach (using a 70:30 weight of GDPIPIFDD and wages) as compared to the one-factor approach (Exhibit J5.2) shows that over the 2007 through 2016 period the annual inflation factors were very similar. However, LPMA notes the wage escalator tends to be more volatile on a year to year basis.

LPMA also notes that an appropriate weighting for labour would need to be estimated. Unlike the 70:30 weighting used for electricity distributors, the weighting would be specific to Amalco and would probably change over the deferred rebasing period as the company changed its operations to find efficiencies. As Mr. Kitchen indicated (Tr. Vol. 5, page 61), the appropriate labour weight for Amalco may be contentious. LPMA further notes that no such weight has been proposed or tested in the current application.

If the OEB were to determine that a two-factor inflation factor was appropriate, then it submits that it should adopt the same timeframe as used for electricity factors in calculating the inflation index to be used each year. This would mean that instead of using the most recent second quarter over second quarter GDP IPI FDD figure from Statistics Canada, the GDP IPI FDD and average wage increase factors should be from the same year and be based on the last full year available from Statistics Canada. Since the average wage figures are only published on annual basis this means, for example, that the inflation factor for 2019 would be based on the 2017 inflation factors since neither of the subcomponents of the two-factor index would be available for 2018 prior to the implementation of the rates on January 1 of 2019.

b. What is the appropriate productivity factor [X]?

The applicants' consultant, National Economic Research Associates Inc., and the OEB staff consultant, Pacific Economics Group Research LLC submitted reports on the appropriate total factor productivity factor. Both consultants recommended 0.0%. LPMA submits that this is an appropriate figure.

c. Should a stretch factor apply and if so, what is the appropriate stretch factor?

LPMA submits that a stretch factor should be applied to ensure some of the up-front savings from the amalgamation are built into rates. This ensures that ratepayers receive a benefit from the proposed merger starting immediately. It provides an additional incentive for Union and Enbridge to find and implement cost saving measures as soon as possible.

LPMA submits that an appropriate stretch factor is 60% of the inflation factor, the same as is currently used in Union IRM.

Both Union and Enbridge have indicated that they have found all of the cost savings that they can as individual companies and the only way to find more savings is for them to amalgamate. LPMA submits that this is nonsense.

If Union and Enbridge are to be believed, then how do they explain their continued over earning throughout the 2014 to 2018 IR period? As shown in the response to Exhibit B.LPMA.18, both Union and Enbridge exceeded their allowed return on equity on a normalized basis in the base year (2013) and each of the four years under their respective IR regimes. Over the 2014 to 2017 period, the average over earning for Union was more than 57 basis points, and for Enbridge was more than 83 basis points.

The average over earning by Enbridge over the 2014 through 2017 period was $23.0 million per year. This can be calculated as the average of the figure shown in the Gross Normalized Over Earnings column for Enbridge shown for 2014 through 2017 in Exhibit JT1.3. With regards to the 2017 estimate shown in that response, Enbridge confirmed it was the final figure in the response to Exhibit J1.2.

Union's normalized over earnings are not shown in Exhibit JT1.3, since Union reported its achieved ROE on an actual basis only. When asked to provide the normalized return on equity and the associated dollar value, the Union witness indicated that is something they would not normally calculate and that it would be a fair bit od work for Union to go back and calculate the figures based on normalized earnings (Tr. Vol. 1, page 134).

However, Union did provide its weather-normalized ROE figures for 2014 through 2017 in Exhibit B.LPMA.18. This information, combined with the information provided in Union's annual deferral account and ESM clearance calculations results in the following normalized over earning figures for Union, which are easily calculated:

2014 - $5.80 million - Source: EB-2015-0010, Exhibit B.CME.1
2015 - $8.07 million - Source: EB-2016-0118, Exhibit B.Energy Probe.8, as calculated
2016 - $14.56 million - Source: EB-2017-0091, Exhibit B.Energy Probe.6, as calculated
2017 - $16.35 million - Source: EB-2017-0307, Tr. Vol. 6, pages 46-47 .

The Union average over the 2014 through 2017 period is $11.2 million.

While the Union figures are approximately one-half of that of Enbridge, it is clear why Union did not want to provide these figures on the record in this proceeding. Unlike the Enbridge over earnings figures which fall in 2015 and 2016 before rising in 2017 from the previous years, the Union figures show a distinct trend. The normalized over earnings for Union have increased each year and in 2017 are nearly three times higher than in 2014.

There is no indication, or evidence, in this proceeding that either Union or Enbridge will suddenly under earn for the first time in a long, long, long time in 2018.

The response to B.LPMA.18 also shows the X factor that was built into rates for each of 2014 through 2017. Because Enbridge was under a Custom IR framework over this period, an X factor is not applicable to Enbridge.

The X factor built into rates was 0.76% in 2014, 1.23% in 2015, 1.19% in 2016, 1.00% in 2017 and 0.76% in 2018 (EB-2017-0087, Exhibit A, Tab 1, page 5). The average over

this five-year period is nearly 1.0% per year (0.988%). Yet each and every year for which we have financial results (2014 through 2017), Union over earned by significant amounts on a normalized basis.

Union has been asked in each of the previous applications to dispose of deferral account balances and earnings sharing applications what the X factor would have had to have been in order to reduce over earnings to zero in each of 2014 through 2016. In EB-2015-0010 Union indicated the X factor would have had to be 1.41%, nearly double the 0.76% included in rates (Exhibit B.LPMA.7). In EB-2016-0118, Union indicated the X factor would have had to be 2.45%, again nearly double the 1.23% included in rates (Exhibit B.Energy Probe.8). In EB-2017-0091, Union indicated the X factor would have to be 3.37%, nearly triple the 1.19% that was built into rates (Exhibit B.Energy Probe.6). For 2017, Union's X factor built into rates was 1.0%, but they over earned by more than any other year under their current price cap IR regime. If the past results are any indication, the X factor needed for 2017 to keep Union at its allowed return on equity would be somewhere between double and triple the actual amount included in rates.

For Union (and Enbridge) to now indicate that they need an X factor (meaning the stretch factor in this context) of 0.00% strains the imagination and the credibility of the companies. If anything, the X factor should be higher than what Union has used during its current price cap IR regime, and even higher for Enbridge, given that its level of over earning has been significantly higher – more than double - than that of Union.

Union's X factor has been calculated as 60% of the inflation rate and in every year for which data is available (2014 through 2017), Union has over earned on a normalized basis. Union's over earning has been steadily increasing over this period.

LPMA submits that there is no credible evidence as to why Union's X factor should not be maintained as 60% of the inflation rate. Union has done well with this X factor, as the over earnings clearly demonstrate. Moreover, Union has done better and better from one year to another under the current mechanism.

It could be argued that Enbridge requires an even larger X factor, given that they have over earned twice as much as Union over the 2014 through 2017 period.

LPMA submits that, as a minimum, the OEB should set the X factor for Amalco as 60% of the inflation rate in recognition of Union being able to achieve and exceed this impact for four consecutive years at an increasing rate and that Enbridge has exceeded even the Union results. Past performance is a good predictor of future performance.

The distributors have fooled the OEB and intervenors in setting the X factor in past proceedings. The OEB should not allow itself to be fooled again.

d. Should there be pass through (Y factor) treatment for costs such as:
i. Gas commodity and upstream transportation costs?
ii. Demand side management (DSM) costs?
iii. A lost revenue adjustment mechanism (LRAM)?
iv. Cap-and-trade costs?
v. Changes to normalized average consumption/average use?

LPMA submits that there should be pass through, or Y factor, treatment for costs related to gas commodity and upstream transportation cots, demand side management costs ("DSM"), cap-and-trade costs and a lost revenue adjustment mechanism "(LRAM"). Each of these costs is treated as pass throughs and LPMA submits that they should continue to be treated in this way during the deferred rebasing period. LPMA also submits that each of these accounts should continue to be treated separately for Union and Enbridge, and where applicable, also for Union South and Union North.

However, LPMA submits that the LRAM should be expanded to include the lost revenues associated with DSM programs for general service customers. The current LRAM only applies to contract rate classes in Union's current IR mechanism. LPMA notes that in the prior five-year price cap IR mechanism, the LRAM did include the DSAM impacts on general service rates.

LPMA submits that the LRAM should include the DSM impacts on general service customers because LPMA does not support the continuance of the changes to normalized average consumption/average use account.

This account was included as part of the overall pack in the settlement agreement that was approved in the EB-2013-0202 Decision and Order dated October 7, 2013 and was explicitly for the 2014 through 2018 period.

In EB-2016-0118, as part of the settlement agreement approved by the OEB in the disposition of deferral account balances proceeding, Union agreed to file a study assessing the continued appropriateness of its methodology for determining the normalized average consumption ("NAC"). To date, Union has not filed this study, but has indicated it will continue to review NAC as a part of Amalco and that changes to NAC, if appropriate, would be considered as part of a future rate proceeding.

LPMA submits that under a price cap mechanism that has not seen any rebasing or comprehensive cost allocation updates since 2011, it is not appropriate to hold the distributor revenue neutral when it comes to weather, while not adjusting the allocation of costs to general service customers to reflect their declining use not only related to annual volumes, but also related to peak day use. In addition, there should be a reflection in the removal of the weather risk from the distributor.

LPMA submits that there should be no volume adjustments made under a price cap IR mechanism given that the distributor is fully protected from all DSM related volumes changes through the LRAM. It is further submitted that making non-DSM related adjustments for only the general service classes is not appropriate. No non-DSM adjustments are made for contract rate classes. No volume adjustments are made for additional volumes achieved through new community expansion projects or transmission and distribution reinforcements that allow additional gas volumes to flow to new and existing customers such as the burgeoning greenhouse industry in the province.

LPMA submits that if the OEB allows Amalco to make volume adjustments for changes in NAC for the general service rate classes, then it should also indicate that adjustments should be brought forward for contract rate classes, new customer additions, new community expansion projects, and so on.

e. Should there be a Z factor, and if so what are the appropriate parameters and materiality threshold?

LPMA supports the continuation of a Z factor for Amalco, but only under certain circumstances.

First, the criteria should be the same as that approved by the OEB in the EB-2013-0202 Settlement Agreement dated July 31, 2013. In particular, for prospective or historical cost increases/decreases to qualify for pass through as a Z factor, 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);
3. not otherwise be reflected in the price cap index;
4. be prudently incurred; and,
5. meet the materiality threshold of annual net delivery revenue requirement impact per Z factor event.

With respect to the materiality threshold, LPMA submits that the $1 million value proposed by Union and Enbridge is significantly too small. In particular, LPMA notes that the current materiality threshold for a Z factor event for Union alone is $4 million.

Given that Amalco will be a little more than twice the size of Union, LPMA submits that an appropriate Z factor materiality threshold for Amalco would be in the $8 million to $10 million range.

f. Should there be an earnings sharing mechanism and if so what are the appropriate parameters?

An earnings sharing mechanism that allows ratepayers to share in the savings is an essential measure to ensure that the no harm test is met. Without the potential for ratepayers to share in potential savings from day 1, there is no adequate protection provided by the Amalco proposal that ratepayers will benefit from reduced costs.

The current proposal for 50/50 sharing between ratepayers and the shareholder **AFTER** five years, and only on earnings **AFTER** Amalco is in excess of the allowed return on equity plus a 300-basis point deadband is, quite frankly, ridiculous and a slap in the face of all ratepayers. While such an approach may be appropriate for the merger of electricity distributors that generally do not have a history of over earning with the frequency and magnitude of Union and Enbridge, it is not appropriate for these two gas distributors.

The evidence in this proceeding is quite clear. The shareholder has indicated that it is happy to take on the amalgamation with its risks and benefits on the expectation that it can earn a return of 20 basis points over the allowed return on equity (Tr. Vol. 1, pages 27-28). If the shareholder is happy with 20 basis points of over earnings, why would the regulator deny a fair and equal sharing of any excess earnings over and above that amount?

LPMA submits that Amalco will have significant incentive to cut costs and earn excess revenues over the allowed return on equity and the 20 basis points noted above. As an example, if Amalco were to earn by 40 basis points over the allowed ROE, 10 basis points would go to ratepayers and the shareholder would retain 30 basis points – a 50% increase over the 20 basis points they would be happy with!

The Union witness indicated that if Amalco were to over earn by more than 20 basis points, that over earning would go back to the benefit of ratepayers at a future point (Tr. Vol. 1, page 28):

> *MR. KITCHEN: Mr. Shepherd, I go back to our original response. The earnings sharing mechanism is intended to provide an incentive to make deep and meaningful savings, and it is also asymmetric. And to the extent that we are able to achieve beyond the 20 basis points over the deferred rebasing period, that, again, will go back to the benefit of ratepayers at a future point.*

LPMA submits that there is no guarantee whatsoever that any over earnings over a ten-year deferred rebasing period will ever be seen by ratepayers. Ratepayers were told the exact same thing as part of the current IR mechanisms in place for the 2014 to 2018 period. Ratepayers were promised savings based on efficiencies gained over this period when the two distributors rebased their rates for 2019. That rebasing is not taking place, so ratepayers will see no benefits of the efficiencies achieved over the 2014 to 2018 period. Oh, and by the way, both distributors over earned significantly on a normalized basis in each and every one of those years for which we have results (see Rate Setting Mechanism Issue #1c above). The promised savings did materialize under the 2014-2018 IR mechanisms. However, they are not flowing through to customers in 2019 as they had been promised. Why should ratepayers now accept the same promise for rebasing in 2029? Fool me once, shame on me; fool me twice, shame on you, and the regulator.

LPMA submits that there should be an asymmetric earnings sharing mechanism that begins in the first year of the deferred rebasing term and applies to every year throughout that period. There would be a 20-basis point deadband of overearning that would accrue to the shareholder, which is all they have indicated that they need to proceed with the amalgamation and to take on the risks associated with the amalgamation. All earnings over and above that level would be shared equally between the shareholder and ratepayers. This approach is fair to both ratepayers and the shareholder.

LPMA further submits that the earnings sharing should be based on weather normalized actual earnings, as it is these earnings, and not weather actual earnings, that will reflect the impact of efficiency gains, synergies and other cost reduction measures achieved as a result of the amalgamation.
LPMA notes that the utility earnings would be calculated excluding the transaction costs associated with the amalgamation. These costs are being tracked separately and are for the account of the shareholder (Tr. Vol. 1, pages 197-198).

An alternative to the above ESM would be to track the transaction costs (which are being tracked by the company anyways) in a deferral account and offsetting those amounts by the level of excess earnings above the allowed return on equity. This would allow Amalco to cover its transaction costs before any sharing with ratepayers would take place. Once it became apparent that the excess revenues were higher than the transaction costs, the excess would be shared on a 50/50 basis with ratepayers. This approach is

similar to the previous approach for an ESM but allows the shareholder to cover their transaction costs quicker and may result in a delay in ratepayers sharing in over earnings. It may also require more regulatory oversight as there may be disagreements over what should and should not be included as transaction costs.

Again, the account would be asymmetric in that sharing would only occur if the accumulated excess earnings were higher than the accumulated transaction costs. If the accumulated transaction costs were higher than the accumulated excess earnings in any year, there would be no sharing of the shortfall. The deficit balance would simply carry on to the following year.

g. Is the proposal for calculating the cost recovery treatment of qualifying capital investments consistent with the OEB's policy for Incremental Capital Modules, and if not are any deviations appropriate?

LPMA's submissions on this issue are limited to the generic issue of the calculation and does not address any specific project or projects. LPMA submits that all projects should be reviewed as part of the application where Amalco brings forward its proposals for ICM adjustments to rates.

LPMA submits that rather than using the ICM, Amalco should use the capital pass-through mechanism that is currently used by Union Gas. This would include the same criteria, including the materiality threshold as are currently applied. The capital pass through materiality threshold differs from that used for the Z factor and should be retained until the next rebasing application.

The capital pass through mechanism has worked well in the current Union IR plan over the entire five-year horizon. It ensures that, on a timely basis, the actual revenue requirement associated with a project is recovered from ratepayers. It provides an excellent level of transparency, as each project that was found to be eligible for a capital pass through mechanism is reported on separately through the annual disposition of deferral and variance account proceedings. It also ensures that new or incremental revenue that results from the project is taken into account in the determination of the net revenue requirement, which is what is recovered from ratepayers, again on an actual basis. The incremental capital module does not take into account additional revenues that may be generated by a project.

Another reason why LPMA believes that the capital pass through mechanism is superior to the ICM is the risk associated with recovery of the costs.

Amalco has indicated that it will follow the OEB's ICM policy which calls for a true-up of the actual revenue requirement and the actual recovery of costs (Exhibit C.LPMA.24, part (a)). This means that regardless of throughput or customer growth, Amalco will recover its actual revenue requirement associated with the capital expenditures included in an ICM. Amalco has no such grand protection on the rest of its rate base. The actual revenue requirement associated with the non-ICM related rate base may be over or under collected based on variations in revenue related to weather, conservation, economic conditions and other influences. Use of the ICM insulates Amalco from those risks, and transfers them to ratepayers. If the weather is warmer than normal, then any shortfall in the recovery of the ICM related revenue requirement is captured through the true up mechanism and results in higher per costs for the ratepayers.

The capital pass through mechanism, however, leaves the risk of recovery of the actual revenue requirement with Amalco, where it belongs, just like the risk of recovery of the non-ICM related rate base. As indicated in the response to part (d) of Exhibit C.LPMA.24, and confirmed at pages 189-190 of the April 3, 2018 Technical Conference transcript, Amalco indicates that under the current capital pass-through mechanism Union is not guaranteed full recovery of any actual revenue requirement. The response goes on to explain this in that the forecast revenue requirements included in the Board-approved rates for capital pass-through projects are subject to volume risk such as weather and that the deferral accounts for capital pass-through projects only record the variance between the forecast costs in rates and the actual costs of the projects. In other words, Union is subject to the same risks on capital pass-through mechanism investments as on investments made outside of the ICM.

The obvious question is why should Amalco, or any distributor, be allowed to earn a return on equity based on the OEB's current cost of capital policy when they have no risk of not recovering their actual revenue requirement associated with the ICM capital? Dire Straits would be impressed…Money for Nothing and the Risks are Free!

The Amalco proposal to use of the ICM appears to be consistent with the OEB's policy for the ICM, with one exception. Amalco proposes to use the then current incremental cost of capital in the calculation of the amounts to be recovered through the ICM, whereas the policy explicitly states that the cost of capital to be used is that embedded in rates. This is clearly stated in Section 7.1.3 Cost of Capital in the EB-2014-0219 Report of the Board: New Policy Options for the Finding of Capital Investments: The Advanced Capital Module. LPMA submits that if the OEB approves the use of the ICM it should retain the use of the cost of capital that is embedded in rates from the last cost of service application.

LPMA is concerned with the calculation of the materiality threshold in the ICM because, for Union in particular, the inputs are from a cost of service proceeding that took place to set 2013 rates. Amalco has indicated that its deviation on the cost of capital parameters that it would use, relative to the OEB policy, is based on the statement at page 15 of Exhibit B, Tab 1, that the OEB's ICM policy was established for five-year ratemaking models, while Amalco would be operating under a ten year deferred rebasing period and using a price cap.

If the OEB determines that this is a legitimate reason to allow Amalco to deviate from the cost of capital parameters to be used, then LPMA submits it is also a legitimate reason to call into question the appropriateness of using 2013 base year figures for the calculation of the materiality threshold. If the ICM policy was established for five year ratemaking, then how can using 5 year old numbers at the **start** of a ten year deferred rebasing period be appropriate, never mind continuing to use them until they are 15 years out of date?

LPMA also submits that the 10% add on factor in the materiality threshold calculation is not appropriate for use by Union or Enbridge. The 10% factor was created based on the electricity distributors in Ontario and not on the gas distributors. A primary difference between these two sectors is that many electricity distributors are seeing limited growth in customer additions, where the gas distributors continue to see strong growth in customer additions, even without the expansion into new communities.

The 10% factor was essentially a stretch factor to ensure that the electricity distributors were held responsible for finding efficiencies to cover the incremental amount of capital spending it represented. Essentially in dollar terms, this factor was 10% of the last approved level of depreciation.

A review of what Union was able to accomplish can be found in the response to Exhibit C.LPMA.23. This interrogatory asked for Union to calculate the materiality threshold for the 2014 through 2018 period and compare that to the actual level of capital expenditures. Union calculated the materiality threshold using the approved parameters from Union's 2013 cost of service proceeding. Line 8 in the table provided shows that in 2015 through 2017 (the years for which we have actual data), Union's actual capital expenditures exceeded the materiality threshold by $51 million in 2014 to $72 million in 2017. The average over this period is $61.75 million. Dividing this figure by the approved 2013 capital expenditures of $196 million (Exhibit B, Tab 1, page 14, Table 1) provides a ration of 31.5%. In other words, Union's capital expenditures were 31.5% above the materiality threshold. Expressed another way, the 10-basis point addition in the materiality threshold formula would have had to been 41.5% for the materiality threshold to match the actual level of capital expenditures over the 2014 through 2017 period.

LPMA submits that this clearly shows that Union was able to survive with capital expenditures significantly and consistently above the materiality threshold for the ICM. Not only did Union survive this period, it actually thrived over the period and consistently over earned in each and every one of the years noted. The level of over earning is discussed in more detail under Rate-Setting Mechanism Issue #1c above. In fact, as noted there, Union's over earning has consistently increased over this period. Clearly capital expenditures significantly in excess of the ICM materiality threshold were no problem for Union in the 2014 through 2017 period. There is no evidence in this proceeding that the same situation would not apply on a going forward basis.

Based on what the historical evidence has shown us, LPMA submits that the materiality threshold formula should replace the 10% factor with a 40% factor to reflect what Union has been able to spend in the recent past without any negative consequences on its financial results. This would increase Union's materiality threshold by $58.8 million (30% x 196 million in depreciation). LPMA further submits that the 40% factor also be applied to Enbridge. Table 1 in Exhibit B, Tab 1, page 14 shows that the materiality threshold calculation for Enbridge is remarkably similar to that of Union, even with the difference in the starting points of the calculations (2013 for Union, 2018 for Enbridge). It would, therefore, be reasonable to assume that an more accurate threshold for Union would also be applicable to Enbridge.

Finally, LPMA proposes a means test be used to determine if rate relief is needed. LPMA proposes that if the normalized earnings of Amalco are more than 100 basis points above the allowed return on equity, then there should be an adjustment to the allowed revenue requirement calculated through the ICM to reflect a reduced need to recover the costs. One hundred basis points is an appropriate deadband for the means test as it is 5 times the 20 basis points over earning that the shareholder is targeting. A means test with a higher deadband than 100 basis points would only mean that the rich would get richer with the blessing of the OEB while ratepayers pay more and more.

2. How should the framework address the four objectives in the Renewed Regulatory Framework of customer focus, operational effectiveness, public policy responsiveness and financial performance?

LPMA believes that its' submissions on other issues effectively address the objectives in the Renewed Regulatory Framework.

The objective of customer focus is addressed through the requirement for a fair earnings sharing mechanism beginning in the first year of the deferred rebasing period, an

achievable stretch factor to ensure that ratepayers receive benefits each and every year, and the continuation of achieving service quality requirements.

Operational effectiveness is addressed by the continuing incentive for Amalco to achieve cost savings in order to achieve its allowed return on equity, plus 20 basis points and 50% of everything over and above that level.

Public policy responsiveness is not impacted by the amalgamation, in the view of LPMA from what would be expected if the two distributors were not to merge. Z factor events are recoverable assuming they meet the criteria. This highlights the need to have a Z factor materiality threshold for Amalco that reflects the relative size of the new company as compared to that of Union. Why should ratepayers be on the hook for additional costs resulting from a change in government policy under Amalco than they would if Union was still a separate company? This could be the result if a Z factor event had a cost of $3 million associated with it, as an example. With a materiality threshold of $4 million, it would not qualify for recovery from Union as a stand-alone distributor, but would quality for recovery from Amalco, with a $1 million materiality threshold even though Amalco is more than twice the size of Union.

Finally, strong financial performance will be encouraged through the shareholder retaining the first 20 basis points of over earnings – an amount that satisfies the Board of Directors – and 50% of any over earnings above that amount.

3. What changes to rates, regulated services, cost allocation or rate design should be permitted or required during the deferred rebasing period and what process should be required for such changes to be made?

LPMA submits that the only changes to rates should be based on the price cap, with the cap being applied equally to all components of the distribution rates such as the fixed monthly charge, the delivery charge, the storage charge and the demand charges.

LPMA submits that the OEB should not allow any changes to cost allocation or rate design without a full cost allocation study. As the OEB is aware, cost allocation is a zero-sum exercise. Shifting costs out of one rate class means that other rate classes will have costs shifted to them. Partial cost allocation that focuses on only 1 or 2 cost drivers is not fair to all customers. Some other cost driver may partially, fully, or more than fully offset the shift in costs for those 1 or 2 particular cost drivers. For example, Union's proposed shift in Panhandle related costs shift costs, in general, from large contract rate classes to the smaller residential and general service customer classes. However, declining average use per customer for these residential and general service customers

may result in a reduction in the quantum of costs allocated to them such as compressor fuel, storage use and even peak day demand and shift those costs to the larger customer classes. The growth in some industries (such as greenhouses) and the decline in others may also have cost allocation consequences that should be recognized as part of a full cost allocation review.

The request for new regulated services, and their costs/rates, should, in the submission of LPMA be permitted within the annual rate filings of Amalco. The request for such services should be subject to full review and scrutiny of intervenors and the OEB before they are approved, modified or denied.

4. What should the annual rate adjustment process be?

In its simplest form, the annual rate adjustment could consist of a rate filing in early September, reflecting the second quarter over section quarter inflation rate from Statistics Canada is available in late August of each year. Such an application would not include any Z factors, cost allocation or rate design proposals, requests for new regulated services or ICM treatment of any projects. This would allow for new rates to be in place by the beginning of the following year.

However, it is not likely that Amalco will be filing a simple annual rate adjustment. It is likely that at least one and possibly more of the ICM, Z factor, cost allocation and/or rate design changes or new regulated services would be included in the filing.

LPMA submits that a September 1 filing that includes any of these addition filing components would not result in rates being reviewed and approved in order to be in place by January 1 of the following year. LPMA also submits that there should be no need for rate retroactivity or the recovery of foregone revenue during a deferred rebasing period.

LPMA submits that in order to effectively review any of the proposed changes, other than the inflation factor, Amalco should be required to file its application and evidence no later than mid June of the year. The inflation factor used should reflect the first quarter over the first quarter information available from Statistics Canada in late March. This filing would allow for the implementation of rates on January 1 of the following year, following a full and comprehensive review of the added adjustments such as an ICM or Z factor request. Filing by mid June would also ensure that the annual filing for the previous year would have been completed and would be under review.

The first quarter over first quarter inflation factor would be a temporary placeholder until the second quarter over second quarter inflation factor was available from Statistics Canada.

5. What deferral and variance accounts should continue?

With the exception of the accounts noted below under Issue #6, LPMA supports the continuation of the deferral and variance accounts listed in Exhibit B, Tab 1, Attachment 4.

However, LPMA submits that there should be more clarity around which accounts apply to which rate zones of Amalco on a going forward basis. For example, both account no. 179.10_ and account no. 179-075 are shown as 'Low Revenue Adjustment Mechanism'.

As well there appear to be accounts that serve the same purpose for Enbridge and Union but have different names. For example, Enbridge has account no. 179.00_ 'Deferred Rebate Account', while Union has account no. 179-132 'Deferral Clearing Variance Account'.

LPMA submits that the OEB should review all accounts that will be continued to ensure that accounts for the current Union and Enbridge distribution areas have appropriate wording where the accounts serve the same purpose.

6. What deferral and variance accounts should not continue?

LPMA has reviewed the accounts proposed to be eliminated, as found in Exhibit B, Tab 1, pages 23-26 and supports the elimination of those accounts.

LPMA also submits that the normalized average consumption/average use related accounts for both Enbridge (179.66_) and Union (179-133) should be eliminated as discussed in more detail under Rate-Setting Mechanism Issue #1d.

7. What additional deferral and variance accounts are appropriate?

LPMA submits that the OEB should establish new accounts or modify existing deferral and variance as required to reflect the OEB's decision in this proceeding. Examples based on the submissions of LPMA would include an account to record earnings sharing.

8. Is the proposed adjustment to reflect the full amortization of Union Gas' accumulated deferred tax balance at the end of 2018 appropriate?

The applicants propose to increase Union's 2018 OEB-approved revenue by $17.4 million pre-tax ($12.8 million after-tax) to recognize the accumulated deferred tax balance credit is fully amortized at the end of 2018 (Exhibit B, Tab 1, page 16).

This credit to ratepayers was the subject of settlement agreements from prior proceedings and the agreements related to this deferred tax balance expire at the end of 2018.

LPMA supports the proposed adjustment, as the settlement agreement that was approved in the EB-2013-0202 Decision and Order dated October 7, 2013 was explicitly for the 2014 through 2018 period.

9. Is the proposed adjustment to unwind smoothing of costs related to Enbridge Gas' Customer Information System and customer care forecast costs appropriate?

LPMA supports the proposed decrease in the OEB-approved revenue of $4.9 million for the reasons set out the in the evidence at Exhibit B, Tab 1, pages 18-20.

10. Is the proposed adjustment to Enbridge Gas' Pension and OPEB costs appropriate?

LPMA supports the proposed increase in the OEB-approved revenue of $6.5 million for the reasons set out the in the evidence addendum in the EB-2017-0307 – Enbridge Gas Distribution Inc. and Union Gas Limited – Rate Setting Mechanism – Evidence Addendum letter dated January 11, 2018.

11. Is the proposed adjustment to reflect the removal of Enbridge Gas' tax deduction associated with the discontinued SRC refund appropriate?

LPMA supports the proposed increase in the OEB-approved revenue of $11.2 million for the reasons set out the in the evidence addendum in the EB-2017-0307 – Enbridge Gas Distribution Inc. and Union Gas Limited – Rate Setting Mechanism – Evidence Addendum letter dated January 11, 2018.

OTHER:

12. Are the provisions of the MAADs Handbook related to harmonization applicable?

LPMA submits that the provisions of the MAADs handbook related to rate harmonization are not applicable. There is no evidence in this proceeding that rates should be

harmonized between the three proposed rate zones. Indeed, as noted earlier in this submission, such a proposal would result in the failure of the no harm test for a significant number of Union customers.

The harmonization of rates can only be reviewed as part of a larger review that includes the harmonization of rate classes and the associated eligibility for those rate classes along with a complete harmonization of cost allocation and rate design methodologies along with such mundane differences between Union and Enbridge with respect to forecast average use per customer, degree day forecasts, peak day determination and so on.

Because of the wide ranging and multitude of things that would need to be addressed, LPMA submits that there should be no harmonization, or even movement towards harmonization, over the deferred rebasing period. It is only at that time, once Amalco has harmonized all other aspects of its operations can the issue of rate harmonization be reviewed.

13. How should past OEB directives and utility commitments be addressed?

LPMA has addressed this issue under MAADs Application Issue #5 above.

14. Is the proposed scorecard appropriate?

LPMA has no specific submissions with respect to the proposed scorecard. However, LPMA does submit that approval of the proposed scorecard in this proceeding should not prevent any party from bringing forward changes or additions to the proposed scorecard during the deferred rebasing period in a future proceeding.

The impacts of the merger are not fully known and may not be known for several years as various departments and functions within Union and Enbridge merge over a relatively long period of time. Parties should be free to bring forward proposals related to the scorecard that may be the result of unforeseen circumstances or events as a result of the merger or changes in the industry.

LPMA does believe that the OEB should give consideration to penalties applicable to Amalco if it fails to meet the standards on any of the items included in the scorecard. This is an important customer protection measure to ensure that financial gains are not coming to the shareholder as a result of deteriorating performance on the scorecard objectives. The penalties, which could be financial in nature, a public reprimand from the OEB, or some other measure would be determined as part of the proceeding in which the scorecard results are filed with the OEB for review.

15. What reporting should be required during the deferred rebasing period?

The applicants have proposed that Amalco will prepare and report on utility information that largely aligns with the schedules provided in Enbridge's 2014-2018 Custom IR proceeding and Union's 2014-2018 IRM proceeding, as listed in Exhibit B, Tab 1, pages 28-29. LPMA submits that the OEB should require the production of these schedules on an annual basis.

In addition, assuming the OEB approves an earnings sharing mechanism beginning in the first year of the deferred rebasing period, LPMA submits that schedules reflecting the calculation and adjustments made to arrive at the earnings sharing amount should be included in the required reporting.

LPMA also supports annual reporting on any material changes associated with work to harmonize the accounting policies of Enbridge and Union. This would include the reporting of all financial impacts of the accounting changes until the policies are fully harmonized and have been implemented. LPMA also agrees with the applicant's proposal to report to the OEB on the net financial impact of the changes when all the changes have been implemented, including any proposed treatment of any material net impact. To be clear, LPMA believes that the net financial impact should be shown on an annual basis as the changes are implemented and not only at the end of the rebasing period.

16. What stakeholder engagement should be required during the deferred rebasing period?

The applicants have proposed that Amalco would host a funded stakeholder meeting every other year starting in 2019. The distributors indicated that preparation of a stakeholder presentation is a significant undertaking and that during such presentations, while there have been some questions, there really has not been enough to talk about, and that more meaningful discussions are likely to occur at stakeholder meetings held every two years rather than every year.

LPMA submits that the OEB should direct Amalco to hold annual funded stakeholder meetings for at least the first five years of the rebasing period.

Unlike past stakeholder meetings, LPMA submits that there will likely be much to discuss with Amalco, not only on the usual topics that are reported on in the stakeholder meetings, but on the progress of the amalgamation, synergies, changes in operations and so on.

LPMA further notes that in its Argument-in-Chief (page 32), Union and Enbridge have indicated that they are open to the suggestion that stakeholder meetings be held annually if this suggestion has general support from intervenors.

D. COSTS

LPMA requests that it be awarded 100% of its reasonably incurred costs. While unable to attend the oral hearing due to prior commitments, LPMA worked with other intervenors throughout the application and hearing process to ensure its areas of concern were examined. This limited duplication while ensuring that the evidentiary record was complete.

ALL OF WHICH IS RESPECTFULLY SUBMITTED
June 15, 2018

Randy Aiken
Consultant to London Property Management Association