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June 15, 2018

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SENT BY EMAIL, COURIER AND FILED ON RESS

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, ON M4P 1E4

Attention: Ms. K. Walli, Board Secretary

Dear Ms. Walli:

EB-2017-0306 and EB-2017-0307
Enbridge Gas Distribution Inc. and Union Gas Limited
Application for Amalgamation and Rate-Setting Mechanism

Please find enclosed herewith City of Kitchener's Final Argument.

Yours very truly,

Richard J. King

RK:hi
Enclosure

c: All Intervenors in EB-2017-0306 and EB-2017-0307

EB-2017-0306
EB-2017-0307

ONTARIO ENERGY BOARD

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

AND IN THE MATTER OF an Application by Enbridge Gas Distribution Inc. and Union Gas Limited, pursuant to subsection 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.

FINAL ARGUMENT OF KITCHENER UTILITIES

June 15, 2018

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OVERVIEW

1. Kitchener Utilities ("**Kitchener**") submits that the Board should: (a) deny the request by Union Gas Limited ("**Union**") and Enbridge Gas Distribution Inc. ("**Enbridge**") (collectively, the "**Applicants**") to defer rebasing until 2029; and (b) order Union to prepare and file a full cost-of-service filing, with a complete cost allocation study, for 2019 rates in accordance with the Settlement Agreement in EB-2013-0202.

2. Kitchener makes these submissions on the following grounds:

   (a) the MAAD policy framework relied on by the Applicants is inapplicable, and the Applicants have not provided sufficient evidence to justify a ten-year deferral period;

   (b) deferring rate rebasing for a further 10 years (on top of the past five years) will unfairly impact the Applicants' ratepayers, including Kitchener; and,

   (c) Union should be required to comply with the terms of its Settlement Agreement in EB-2013-0202.

3. Kitchener takes no position on the relief requested by the Applicants under subsection 43(1) of the *Ontario Energy Board Act, 1998* (the "OEB Act") for approval to amalgamate.

4. In addition, as a large customer of Union (and not Enbridge), Kitchener's submissions are directed at the Applicants' rebasing proposal as it applies to Union, recognizing that this proceeding is a joint application.

DISCUSSION

The MAAD Handbook is not applicable to the deferred rebasing proposal

5. It is important to consider the proper basis for the Applicants' request to defer rebasing for a period of ten years. Proposed as part of the Applicants' application in EB-2017-0306 (the "**Amalgamation Application**"), it was assumed by the Applicants that they were entitled *as of right* to select their preferred rebasing deferral period. This was based on the Applicants' assumption that the OEB's *Handbook to Electricity Distributor and Transmitter Consolidations* (the "**MAAD Handbook**") was applicable to the Amalgamation Application.

6. The Board, in Decision and Procedural Order No. 3, determined that the OEB's MAAD Handbook does not automatically apply to the Amalgamation Application, and as a result, the Applicants' are not entitled to select a deferral period of up to 10 years as of right:

> 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 ... are legitimate areas of inquiry and are not pre-determined.** ... (emphasis added)
>
> (OEB Decision and Procedural Order No. 3, EB-2017-0306/0307, p.6)

7. The Board's decision is straightforward – when it comes to the appropriateness of a rebasing deferral period in the context of an amalgamation, the MAAD Handbook does not pre-determine the issue.

8. The Applicants, then, bear the burden of justifying a proposal that would enable both utilities (collectively serving nearly all Ontario natural gas customers) to avoid rebasing for what will be a 15 year period. From a regulatory perspective, that burden should be significant.

9. It is Kitchener's submission that the Applicants have failed to discharge that burden.

10. Indeed, the Applicants offer two main justifications for the 10 year deferral period: (a) the MAAD Handbook applies[1] to the Amalgamation Application; and (b) a ten year period is required to successfully integrate the two utilities.

11. In Kitchener's submission, these justifications miss the point. Further, intervenors such as Kitchener have brought forward significant cost allocation issues that exist now, that would be only further exacerbated by a failure to rebase rates immediately. There has been no satisfactory evidence from the Applicants on these issues.

12. The Applicants' evidence on the nature of effort to successfully integrate the two utilities is only half of what the Board needs to consider – the other half being the harm to ratepayers of a further ten years of disconnect between utility costs and rates. On this point, there is no mitigation plan from the utilities.

Deferring rebasing for a further 10 years will unfairly impact Kitchener and other ratepayers

13. Kitchener is one of Union's largest customers, and is the only customer in Union's Rate T3 class. In the past five years (i.e., since Union's last rebasing), Union's T3 monthly transportation demand charge has increased from 9.3582 cents/m^3 to 17.9898 cents/m^3. This is a 92% increase over a five year period.

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[1] See paragraphs 34 to 38 of the Applicants' Argument-in-Chief. In those paragraphs, the Applicants reiterate their Draft Issues List submission's convoluted narrative by which they attempt to bring the rebasing deferral proposal within the scope of the MAAD Handbook. We will not reiterate our arguments made in response to the Applicants' Draft Issues List submission on this point, but have excerpted them and attached them as Appendix A hereto for convenience.

14. The 92% increase is primarily due to the addition of capital pass-through costs associated with a few large projects (the "**Large Projects**"), which have been reflected in rates almost entirely in the last three years.

15. Kitchener began actively disputing Union's allocation of these project costs approximately five years ago in Union's leave-to-construct proceedings.[2] In response to Kitchener's cost allocation concerns, the Board stated:

> **The considerations that Kitchener has raised would require a broader examination of cost allocation principles and their application to the Dawn-Parkway system, which is beyond the scope of this proceeding.** Kitchener proposed that the Board conduct a separate review using a consultation process. In the normal course, cost allocation issues are reviewed in cost of service rebasing hearings. The Board finds that Kitchener has not made a sufficiently compelling case to warrant a stand-alone review of the issue, **but this issue could be raised in Union's next cost of service proceeding.**[3] (emphasis added)

16. At the time of the issuance of this Decision, Union had committed itself in a Board-approved Settlement Agreement, to file a cost-of-service application for 2019 rates.

17. While at the time Kitchener was disappointed at the prospect of having to wait four to five years to resolve these cost allocation issues, it did have an expectation (based on the Board's Decision and Union's commitment in the Settlement Agreement) that the rate shocks associated with these projects would persist perhaps for only two or three years. That is no longer the case. Given that there will be no rebasing by Union for 2019 rates, the rate shocks will persist for twelve to thirteen years.

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[2] EB-2012-0433 (Parkway West)/EB-2013-0074 (Branford-Kirkwall/Parkway D) – heard with Enbridge's EB-2012-0451.

[3] OEB Decision in EB-2012-0433/EB-2013-0074/EB-2012-0451 dated January 30, 2014.

18. The Applicants have indicated that Kitchener would not be precluded from bringing forward cost allocation issues at annual rate adjustment proceedings prior to 2029[4], but would object to any resultant rate changes applying retroactively:

> MR. KING: ... Would Amalco object to consumers bringing forward cost allocation proposals in these annual rate applications for any past projects back to your last rebasing?
>
> MR. KITCHEN: ... I would say we would only oppose it if it was related to a prior project and it was retrospective in nature. If it was proposed on a prospective basis, then I don't think I can object to a customer bringing forward a concern about cost allocation.

19. At best, then, Kitchener would have to bring forward a successful cost allocation case in some future annual rate case in order to adjust rates going forward.

20. Notwithstanding Union's position that an annual rate adjustment proceeding could provide a forum for customer cost allocation issues, Kitchener is skeptical that the Board would entertain cost allocation adjustments at annual rate adjustments prior to 2029, based on Board pronouncements in the very recent past. In Union's last rate application (EB-2017-0087), the issue of allocating the reinforcement costs associated with the Panhandle Reinforcement Project was raised by IGUA, and the Board was clear in its views on cost allocation issues associated with projects being dealt with between rebasing applications:

> The allocation of the Panhandle Reinforcement Project costs for 2018 was an unsettled issue in the settlement agreement. By Procedural Order 3, the OEB had ruled that changes to the existing cost allocation methodology would not be considered in this hearing that concerns the last year of the IRM.

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[4] At Exhibit C.Kitchener Utilities.5(d), the Applicants were asked to "confirm that if the Applicants' rebasing proposal is accepted by the Board, Kitchener Utilities would be precluded from raising their cost allocation concerns with respect to the Large Projects". In response, the Applicants stated: "Not Confirmed. Kitchener Utilities may bring forward its concerns about cost allocation in the annual rate setting process."

> IGUA urged that the OEB consider mechanisms other than changes to the cost allocation methodology to address what it maintained was an inequitable result of the existing cost allocation methodology approved by the OEB in 2013. ...
>
> **Findings**
>
> ... **The OEB is of the view that any change to the existing cost allocation model should be done with the assistance of a comprehensive system-wide full cost allocation study. Cost allocation is a zero sum exercise. A full study ensures that all changes to facilities, operations and use in the transmission system since the development of the previous cost allocation model are recognized across all customer classes.** This form of study provides that positive and negative changes in costs throughout the system are accounted for. A finding that current rates are inequitable because of the underlying allocation of costs for one project could introduce other inequalities by an incomplete analysis of the changing cost impacts on customers. **Equitable cost causality is only possible with a full study.**[5] (emphasis added)

21. These are the same Panhandle costs that Union is seeking to adjust in this proceeding, in the absence of a full cost allocation study.

22. Kitchener seeks the Board's guidance on this issue. Kitchener has been operating on the understanding that cost allocation issues associated with past projects (such as the Large Projects) can only be dealt with at a rebasing application. That is what Kitchener was told in January 2014 (in EB-2012-0433/EB-2013-0074/EB-2012-0451) and it is the very clear message from the Board in January of this year (in the excerpt from the OEB Decision in EB-2017-0087 above).

23. Based on that, the impact of the Applicants' rebasing deferral proposal would be to enshrine the significant rate increases associated with the Large Projects in Kitchener's rates for a further ten years, with no ability for Kitchener to seek redress.

The Board should require Union to honour with the Settlement Agreement in EB-2013-0202

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[5] OEB Decision, EB-2017-0087, p. 5 and 8.

24. Kitchener was a party to the Settlement Agreement in Union's Incentive Rate Mechanism application to set rates for the 2014 to 2018 period. That Settlement Agreement was accepted by the Board.

25. Section 14 of that Settlement Agreement states as follows:

> **REBASING**
>
> Union agrees (**subject to any subsequent agreement of all parties to extend** the IRM term) to prepare a full cost of service filing at the time of rebasing, **regardless of whether Union applies to set rates for 2019 on a cost of service basis or not**. (emphasis added)

26. This wording is both unusual and unequivocal. Union's obligation to prepare and file a full cost of service filing: (a) applies regardless of whether Union applies to set 2019 rates on a cost of service basis or via some other methodology; and (b) can only be varied with the agreement of all parties to the Settlement Agreement.

27. It is clear from the these two qualifiers that intervenors participating in that Settlement Agreement saw the rebasing at the end of the IR term as key – applicable even if some other rate-setting methodology was brought forward, and only to be varied with the concurrence of all intervenors.

28. Kitchener is asking the Board to hold Union to its commitment. All parties that participate in the Board's settlement processes should be able to rely on the promises exchanged in the course of settlement conference processes.

29. Moreover, Union should not be able to rely on an argument that suggests that the circumstances presented by the amalgamation are so extraordinary that Union should be relieved

of their obligation. The two qualifiers in section 14 of the Settlement Agreement are the answer to such an argument. The intent was clearly to indicate that whatever the intervening circumstances, the parties require cost-of-service information in 2019. Union agreed.

30. The Board should be concerned about the efficacy and integrity of its settlement processes. To relieve Union of its obligation to make a cost-of-service filing for 2019 would send a message to utilities and intervenors that Settlement Agreements (and the bargains made therein) cannot be fully relied upon. That would, in Kitchener's view, change intervenors' approach to settlement in an adverse way – making settlement less likely.

CONCLUSION

31. Kitchener respectfully submits that the Applicants' proposal to defer rebasing until 2029 should be denied.

32. Further, Kitchener submits that the Board should order Union to prepare and file a full cost-of-service filing, with a complete cost allocation study, for 2019 rates in accordance with the Settlement Agreement in EB-2013-0202.

ALL OF WHICH IS RESPECTFULLY SUBMITTED,

June 15, 2018

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Counsel for Kitchener Utilities

APPENDIX A

Excerpt of Kitchener's Submission on Issues List (February 2, 2018)

The Applicant views deferred rebasing as an election that it may exercise in its sole discretion:

> In light of the guidance provided by the Board for consolidation applications, **there is no legitimate issue in this case about the deferred rebasing period**. The Board's policy is that the extent of the deferred rebasing period is at the option of the distributor and that no supporting evidence is required to justify the selection of the deferral period.[6]
>
> [emphasis added]

This assertion of the Applicant boldly states that if a merger is approved, then deferred rebasing is a right that is beyond the scrutiny of the Board or others. The purported authority for this right is the Board's *Handbook to Electricity Distributor and Transmitter Consolidations*, January 19, 2016 (the "**Consolidation Handbook**").[7]

Kitchener Utilities submits that the Applicant has misinterpreted the applicability of the Consolidation Handbook to the amalgamation under consideration. As a starting point, the Consolidation Handbook is, by its very title, applicable only to *electricity distributors and transmitters*.

The convoluted path by which the Applicant attempts to bring itself within the scope of the Consolidation Handbook (for the purposes of deferred rebasing) originates in the Board's *Handbook for Utility Rate Applications*, October 13, 2016 (the "**Rate Handbook**").[8] The link between the Rate Handbook and the deferred rebasing provisions of the Consolidation Handbook is tenuous at best, and its weaknesses are self-evident when one attempts to follow the Applicant's logic. One only need to look at the stated purpose of deferred rebasing (as set out in the portion of the Consolidation Handbook that the Applicant relies on as authority for deferred rebasing) to demonstrate that deferred rebasing as of right is not appropriate for gas distributors:

> **To encourage consolidations**, the OEB has introduced policies that provide consolidating distributors with an opportunity to offset transaction costs with any achieved savings. The 2015 Report permits consolidating distributors to defer rebasing for up to ten years from the closing of the transaction… The extent of the deferred rebasing period is at the option of the distributor and no supporting evidence is required to justify the

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6 Applicant's Argument-In-Chief on Issues List in EB-2017-0306 at para 38.

7 Applicant's Argument-In-Chief on Issues List in EB-2017-0306 at para 34.

8 Applicant's Argument-In-Chief on Issues List in EB-2017-0306 at paras 8-9.

> selection of the deferred rebasing period subject to the minimum requirements set out below.[9]
>
> [emphasis added]

The opening words of this excerpt are instructive – the purpose of deferred rebasing is to *encourage consolidations*. This is clearly meant for electricity distributors and not gas distributors. It has long been a provincial and OEB policy to encourage electricity distribution consolidation. There has been no policy aimed at merging EGD and Union.

The passage from the Consolidation Handbook excerpted above flows from prior OEB processes – all aimed at electricity distributor consolidation. The "2015 Report" noted n the excerpt (which "permits consolidating distributors to defer rebasing for up to ten years…") is a reference to the *Rate-making Associated with Distributor Consolidation* Report of the Board, (EB-2014-0138) March 26, 2015. That Report focused on incentivizing *electricity* consolidation, noting:

> The report of the Ontario Distribution Sector Review Panel, issued in December 2012, set out a vision for **consolidation resulting in the less costly and more efficient delivery of electricity**, with a predicted cost savings of $1.2 billion over the next ten years. When the Minister of Energy responded to the Panel's report, he indicated that he expected that the sector would find ways to achieve those savings through more efficient service delivery, including negotiated consolidations.[10]
>
> [emphasis added]

The 2015 Report specifically notes that "[t]he OEB's current policy with regards to issues associated with MAADs transactions was developed in 2007, and is found in its *Report of the Board regarding Rate-making Policies Associated with Distributor Consolidation*",[11] dated March 5, 2007 (the "**2007 Policy**"). The 2007 Policy specifically notes:

> Consolidation may take a number of forms. **The proposals set out in this paper apply only to transactions where two or more distribution companies come together through a transaction (such as an amalgamation) that results in a single, rate-regulated licensed electricity distributor. References in this paper to "distributor consolidation" should be interpreted accordingly**.[12]
>
> [emphasis added]

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9 Consolidation Handbook at 11-12.

10 2015 Report at 3.

11 2015 Report at 5.

12 2007 Policy at 1.

The 2007 Policy was a precursor to the *Rate-making Associated with Distributor Consolidation* Report of the Board, July 23, 2007 (the "**2007 Report**"), which notes:

> Earlier this year, the Board initiated a consultative process focusing on the regulatory treatment of certain rate-related issues associated with **consolidation in the electricity distribution sector**.[13] ... **The policy set out in this Report applies to transactions between electricity transmitters that result in a single, rate-regulated licensed electricity distributor** (the "consolidated entity").[14]
>
> [emphasis added]

The consistent policy demonstrated by the 2007 Policy, 2007 Report, 2015 Report, and the Consolidation Handbook is that the purpose of deferred rebasing is to incentive the consolidation of electricity distribution companies. There is no evidence, indication or support that gas distributors are eligible for deferred rebasing, for the simple reason that the government has not been seeking the consolidation of gas distributors. Based on the foregoing, the Applicant is either mistaken or engaging in obfuscation when it states:

> In light of the guidance provided by the Board for consolidation applications, there is no legitimate issue in this case about the deferred rebasing period. The Board's policy is that the extent of the deferred rebasing period is at the option of the distributor and that no supporting evidence is required to justify the selection of the deferral period.[15]

Kitchener Utilities submits that merging natural gas distributors are not entitled to deferred rebasing as of right.

This is supported not only by the Board's own documents, but also by recent precedent. The Applicant notes that in developing the Applicant Issues List that it was guided by the Board decision in EB-2016-0351,[16] which approved the sale of Natural Resource Gas Limited's distribution system to EPCOR Natural Gas Limited Partnership (the "**NRG/EPCOR Decision**"). This has been the only recent MAAD application in the natural gas sector to speak of. At the time of the MAAD application, NRG had come to the end of its incentive rate-making term and had recently filed a re-basing application. It is noteworthy that the NRG/EPCOR Decision did not consider deferred rebasing. Indeed, part of the Board's decision to approve the transaction was based upon EPCOR's commitment to file an amended rate application within 6 to 9 months of the

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13 2007 Report at 1.

14 2007 Report at 3.

15 Applicant's Argument-In-Chief on Issues List in EB-2017-0306 at para 38.

16 Applicant's Argument-In-Chief on Issues List in EB-2017-0306 at para 17.

closing of the transaction.[17] As such, the NRG/EPCOR Decision supports Kitchener Utilities' position (and that of other Intervenors) that deferred rebasing is not an entitlement in this case.

Instead, the issue for this proceeding is whether it is appropriate to defer rebasing of the merged utility (assuming approval is granted) for ten years, some other period of time, or at all. It is Kitchener Utilities' position that the Applicant bears the burden of demonstrating that such deferral is warranted having regard to, *inter alia*, ratepayer protection, the fact that the Applicant's current proposal would allow for a fifteen year period between rebasings, and the Board's statutory objectives with respect to gas.

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[17] NRG/EPCOR Decision at 4.