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Ontario

ONTARIO ENERGY BOARD

OEB STAFF SUBMISSION

Union Gas Limited

Application for disposition and recovery of certain 2017 deferral account balances and approval of the earnings sharing amount

EB-2018-0105

October 3, 2018

Background

Union Gas Limited (Union) filed an application with the Ontario Energy Board (OEB) on June 6, 2018 for approval to dispose of and recover certain 2017 deferral account balances.

The total net balance of these deferral accounts is a recoverable from ratepayers of $2.2 million. Union has indicated that its 2017 actual utility earnings did not exceed the threshold established in Union's 2014-2018 Incentive Regulation proceeding[1] and therefore there is no sharing of earnings with ratepayers.

In accordance with Procedural Order No. 1, a settlement conference was held on September 4 and 5, 2018. By letter dated September 12, 2018, Union advised the OEB that there was no settlement proposal resulting from the settlement conference. Union requested that the OEB provide the opportunity for written submissions from intervenors and OEB staff followed by a reply submission.

In Procedural Order No. 2, the OEB scheduled deadlines for the filing of written submissions by intervenors and OEB staff and a reply submission by Union.

OEB Staff Submission

OEB staff's submission is set out in the sections that follow. OEB staff will argue for changes to the balances requested for disposition in two accounts (the Lobo D / Bright C / Dawn H Compressor Project Costs Deferral Account and the OEB Cost Assessment Variance Account). OEB staff will also provide a brief overview of the other accounts for which Union seeks disposition as part of the current proceeding, the proposed earnings sharing amount, the proposed allocation of balances in the deferral and variance accounts and the proposed disposition methodology.

Summary of Proposed Disposition

Union is requesting approval to dispose of balances in certain 2017 deferral and variance accounts. The net balance in the various deferral accounts is a debit balance of $2.2 million as at December 31, 2017 (including interest).

[1] EB-2013-0202.

	DEFERRAL AND VARIANCE ACCOUNTS		
	GAS SUPPLY ACCOUNTS		
	Account #	**Account Name**	**Balance ($000's)**
	179-107	Spot Gas Variance Account	-
	179-108	Unabsorbed Demand Cost Variance Account	(4,159)
	179-131	Upstream Transportation Optimization	11,057
	179-132	Deferral Clearance Variance Account - Supply	320
	179-132	Deferral Clearance Variance Account - Transport	507
		Total Gas Supply Accounts	**7,725**
	STORAGE ACCOUNT		
	179-170	Short-Term Storage and Other Balancing Services	1,183
	OTHER ACCOUNTS		
	179-103	Unbundled Services Unauthorized Storage Overrun	-
	179-112	Gas Distribution Access Rule Costs	76
	179-120	IFRS Conversion Costs	-
	179-123	Conservation Demand Management	(245)
	179-132	Deferral Clearance Variance Account - Delivery	1,763
	179-133	Normalized Average Consumption	(2,914)
	179-134	Tax Variance	(331)
	179-135	Unaccounted for Gas Volume Variance Account	-
	179-136	Parkway West Project Costs	(528)
	179-137	Brantford-Kirkwall/Parkway D Project Costs	(868)
	179-138	Parkway Obligation Rate Variance	(121)
	179-139	Energy East Pipeline Consultation Costs	-
	179-141	Unaccounted for Gas Price Variance Account	103
	179-142	Lobo C Compressor/Hamilton-Milton Pipeline Project Costs	(6,327)
	179-143	Unauthorized Overrun Non-Compliance Account	(8)
	179-144	Lobo D/Bright C/Dawn H Compressor Project Costs	4,918
	179-149	Burlington-Oakville Project Costs	(3,477)
	179-151	OEB Cost Assessment Variance Account	1,167
	179-153	Base Service North T-Service TransCanada Capacity	-
	179-156	Panhandle Reinforcement Project Costs	83
		Total Storage & Other Accounts	**(5,526)**
		TOTAL DEFERRAL ACCOUNT BALANCES	**2,199**

Deferral and Variance Accounts for which a reduction to the balance is appropriate

Lobo D / Bright C / Dawn H Compressor Project Costs Deferral Account

The account tracks the difference between the actual revenue requirement related to costs associated with the Lobo D / Bright C / Dawn H project and the revenue requirement included in rates. The deferral account has a debit balance of $4.912 million, plus interest of $0.006 million for a total balance of $4.918 million. The debit balance is largely driven by the assets being put into service earlier than the forecast in-service date.[2]

In the 2017 Dawn Parkway Project approved settlement proposal, Union noted that it expects to be in a slight surplus capacity position of 30,393 GJ/d on the Dawn Parkway system upon the completion of the project. Union further stated that it will actively market the surplus capacity and that the revenues from such marketing will be credited to the proposed Lobo D / Bright C / Dawn H Compressor Projects Costs Deferral Account.[3]

In response to an OEB staff interrogatory, Union explained that it included the delivery revenue requirement of the project in 2017 Rates, which excluded the revenue associated with the 30,393 GJ/d of surplus capacity associated with this project. Union stated that if it experiences surplus capacity in excess of 30,393 GJ/d due to expiring contracts or adjustments to total system capacity, revenue obtained by selling that capacity forms part of utility earnings and is subject to earnings sharing. Once all surplus capacity in excess of 30,393 GJ/d has been sold on a long-term basis, any further sales will then be applied to the Lobo D / Bright C / Dawn H Compressor Project Costs Deferral Account. As Union's actual Dawn to Parkway surplus for winter 2017 / 2018 was in excess of 30,393 GJ/d, there was no long-term Dawn-Parkway revenue to apply to the Lobo D / Bright C / Dawn H Compressor Project Costs Deferral Account.[4]

OEB staff understands Union's position to be that only after it sells all of its surplus capacity on the Dawn Parkway system that is related to assets other than the Lobo D / Bright C / Dawn H compressor project will any amount be credited to the noted deferral account. Union has essentially separated its surplus capacity as between Lobo D / Bright C / Dawn H project-related capacity and the capacity related to all of its other Dawn Parkway system assets.

[2] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 1 / pp. 50-58.
[3] EB-2015-0200, Settlement Agreement, p. 8.
[4] EB-2018-0105, Interrogatory Responses, OEB Staff-13, p. 2.

OEB staff submits that the manner in which Union proposes to determine whether revenues are generated from the 30,393 GJ/d of surplus capacity associated with the noted project is not appropriate.

OEB staff submits that Union has a portfolio of assets that comprise the Dawn Parkway system, which includes the Lobo D / Bright C / Dawn H assets. All of the assets in combination result in the surplus capacity available on the Dawn Parkway system. There is no reason that the sale of the surplus capacity associated with the Lobo D / Bright C / Dawn H compressor project should be deprioritized relative to its other Dawn Parkway system assets when calculating the balance in the Lobo D / Bright C / Dawn H Compressor Project Costs Deferral Account.

For these reasons, OEB staff submits that the OEB should order Union to calculate the revenue to be included as an offset to the balance in the Lobo D / Bright C / Dawn H Compressor Project Costs Deferral Account on the basis of a proration of the total revenues generated through Dawn Parkway surplus capacity. Specifically, Union should divide the total surplus capacity on the Dawn Parkway system by the 30,393 GJ/d that was created by the Lobo D / Bright C / Dawn H project. The revenue generated from surplus capacity on the Dawn Parkway system should be multiplied by the proportion (percentage) of the total surplus that is associated with the Lobo D / Bright C / Dawn H project and this amount should be recorded as an offset in the deferral account.

OEB staff notes that for the purposes of this calculation in 2017, the total revenue amount should only include revenues generated after the Lobo D / Bright C / Dawn H project came into service. In future years, full year revenues are appropriate.

Ontario Energy Board Cost Assessment Variance Account

On February 9, 2016, the OEB issued a letter to regulated entities subject to the OEB's cost assessment notifying stakeholders of changes to the OEB's Cost Assessment Model (CAM). As part of these changes, the OEB established a variance account to record any material differences between OEB cost assessments currently built into rates, and cost assessments that will result from the application of the new CAM effective April 1, 2016.[5]

[5] OEB Letter, Re: Revisions to the Ontario Energy Board Cost Assessment Model, February 9, 2016, p. 2.

Currently, $2.5 million in OEB assessment costs are included in Union's rates. In 2017, the actual amount of cost assessment was $3.659 million. As such, the balance in the account requested for clearance is a debit from ratepayers of $1.159 million plus interest of $0.008 million for a total of $1.167 million.[6]

OEB staff submits that the language in the letter establishing this variance account is clear that the account is only intended to record "any material differences."

OEB staff notes that there are two different materiality thresholds that could be used in determining whether the amount sought for clearance in the noted variance account is material to Union.

First, Union has a Z-factor materiality threshold applicable to its 2014-2018 IRM term of $4.0 million.[7] OEB staff notes that the settlement agreement describes the types of costs that would qualify for Z-factor treatment as those that are: (a) causally related to an external event that is beyond management's control; (b) result from a type of risk that a prudent utility would not be expected to take mitigation steps; (c) not otherwise reflected in the price cap index; and (d) be prudently incurred.[8]

OEB staff notes that Z-factor treatment has typically been applied by the OEB to costs that were related to storm damage. However, OEB staff submits that the changes to the CAM seem to fit the criteria for Z-factor treatment. In the absence of the OEB establishing a specific deferral account to address these cost changes, OEB staff is of the view that utilities could have brought forward these incremental costs as Z-factor claims. For that reason, OEB staff believes that the Z-factor materiality threshold is a reasonable threshold to use in determining whether the balance in this account is material to Union.

The second materiality threshold that could be viewed as relevant to determining whether the amount recorded in the variance account is material is the threshold for establishing new deferral and variance accounts. As set out in the OEB's Filing Requirements for Natural Gas Rate Applications, the materiality threshold for establishing new deferral and variance accounts is $1.0 million for a utility with a

[6] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 1 / pp. 63-64.
[7] EB-2013-0202, Settlement Agreement, Exhibit A / Tab 1 / p. 36.
[8] EB-2013-0202, Settlement Agreement, Exhibit A / Tab 1 / pp. 35-36.

revenue requirement of more than $200 million.[9] OEB staff submits the filing requirements were issued after the OEB Cost Assessment Variance Account was established and are designed to be prospective (and intended to provide information about the requirements for a cost of service application).[10] OEB staff submits that as the establishment of the noted account predates the issuance of the filing requirements, the materiality threshold contained in the requirements should only be viewed as potential guidance.

OEB staff notes that the balance in the account falls between the two thresholds that could be used to determine materiality. The balance of $1.167 million is well below the Z-factor materiality threshold and only slightly higher than the threshold for establishing deferral and variance accounts. Taking a balance of the thresholds, OEB staff submits that the amount is not material. For that reason, OEB staff submits that the OEB should order that the $1.167 million balance in the account not be eligible for recovery from ratepayers.

OEB staff notes that the OEB Cost Assessment Variance Account has not previously been disposed as Union agreed to not recover the 2016 balance in this account. The balance in the account was a debit of $0.832 million in 2016.[11]

Deferral and Variance Accounts for which no adjustments to the balance is required

OEB staff submits that the balances in all of the following accounts have been calculated correctly and the amounts sought for disposition should be approved by the OEB.

- Spot Gas Variance Account (no balance)
- Unabsorbed Demand Cost Variance Account
- Upstream Transportation Optimization
- Deferral Clearance Variance Account
- Short-Term Storage and Other Balancing Services
- Unbundled Services Unauthorized Storage Overrun (no balance)
- Gas Distribution Access Rule Costs

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[9] Ontario Energy Board, Filing Requirements for Natural Gas Rate Applications, February 16, 2017, Chapter 2, p. 38.
[10] Ontario Energy Board, Filing Requirements for Natural Gas Rate Applications, February 16, 2017, Chapter 1, p.1.
[11] EB-2017-0091, Updated Settlement Proposal, p. 17.

- IFRS Conversion Cost (no balance)
- Conservation Demand Management
- Normalized Average Consumption
- Tax Variance
- Unaccounted for Gas Volume Variance Account (no balance)
- Parkway West Project Costs
- Brantford-Kirkwall/Parkway D Project Costs
- Parkway Obligation Rate Variance
- Energy East Pipeline Consultation Costs (no balance)
- Unaccounted for Gas Price Variance Account
- Lobo C Compressor/Hamilton-Milton Pipeline Project Costs
- Unauthorized Overrun Non-Compliance Account
- Burlington-Oakville Project Costs
- Base Service North T-Service TransCanada Capacity (no balance)
- Panhandle Reinforcement Project Costs

OEB staff notes that the Parkway West Project Costs Account tracks the difference between the actual revenue requirement related to costs for the Parkway West Project and the revenue requirement included in rates. The balance in the Parkway West deferral account is a credit to ratepayers of $0.526 million plus interest of $0.002 million for a total of $0.528 million.[12]

In the 2016 deferral account disposition proceeding[13], all parties agreed that the 2016 balance in the Parkway West Project Costs Account should be disposed of only on an interim basis to allow the OEB to perform a prudence review of the capital overspend in the future prior to final disposition of the balances in the account.[14] In the current application, Union proposed that the balance in the account continue to be disposed of on an interim basis (consistent with the approval granted in the 2016 deferral account disposition proceeding).[15] OEB staff submits that the OEB should accept Union's proposal to continue disposing of this account on an interim basis. OEB staff notes that Union advised that it will likely file the evidence with respect to the prudence review in 2020.[16]

[12] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 1 / pp. 28.
[13] EB-2017-0091.
[14] EB-2017-0091, Updated Settlement Proposal, p. 12.
[15] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 1 / pp. 29.
[16] EB-2018-0105, Interrogatory Responses, OEB Staff-10, p. 2.

OEB staff notes that this application is the first time that Union is seeking recovery of the balance in the Panhandle Reinforcement Project Costs Account. The account tracks the difference between the actual net revenue requirement related to costs for the Panhandle Reinforcement Project and the net revenue requirement included in rates. The deferral account balance is a debit from ratepayers of $0.083 million. This represents the total 2017 actual net revenue requirement related to this project as no amount was included in rates for 2017.[17] OEB staff submits that the balance in the account has been calculated correctly and should be approved for recovery from ratepayers.

Earnings Sharing Mechanism

As per Union's approved settlement proposal in the 2014-2018 Incentive Regulation proceeding[18], Union did not exceed the return on equity (ROE) threshold and therefore there is no earnings sharing with ratepayers. If the difference between the actual ROE and the benchmark ROE is greater than 100 basis points but less than 200 basis points, the excess earnings are shared 50/50 between Union and its ratepayers. If the difference between the actual ROE and the benchmark ROE is greater than 200 basis points, the excess over 200 basis points is shared 90/10 to the benefit of ratepayers. For 2017, the difference is 23 basis points and therefore there is no earnings sharing.[19]

OEB staff notes that the earnings sharing calculation includes $5.6 million of merger-related costs (and $3.7 million of related savings) associated with the Enbridge Inc. and Spectra Energy merger.[20] In response to an interrogatory, Union provided the earnings sharing calculation with the $5.6 million merger-related costs removed (but maintaining the $3.7 million savings in the calculation). The result of that calculation is that there are still no earnings to be shared with ratepayers (as Union is still below the threshold for sharing).[21]

OEB staff submits that the OEB should accept the 2017 earnings sharing calculation as the inclusion of merger-related costs has no impact on the amount to be shared. In the

[17] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 1 / pp. 64-65.
[18] EB-2013-0202, Settlement Agreement, Exhibit A / Tab 1 / p. 37.
[19] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 2 / p. 8.
[20] OEB staff notes that the earnings sharing calculation excludes $0.18 million of legal costs associated with the Union Gas Limited / Enbridge Gas Distribution Inc. merger application. EB-2018-0105, Interrogatory Responses, IGUA-1, p. 1.
[21] EB-2018-0105, Interrogatory Responses, Staff-16.

future, if the merger-related costs impact the amount of earnings to be shared, further discovery of this issue will occur and OEB staff may seek to argue about the appropriate treatment.

Allocation of 2017 Deferral and Variance Account Balances

OEB staff has no concerns with Union's proposed allocation of 2017 deferral account balances. With two exceptions, the allocation of 2017 deferral account balances to rates classes is consistent with the allocations previously approved by the OEB in Union's 2016 Deferral Account Disposition Proceeding[22], Union's 2013 Cost of Service Proceeding[23] or Union's Dawn Reference Price proceeding.[24,25]

The OEB Cost Assessment Variance Account and Panhandle Reinforcement Project Costs Deferral Account have not been previously disposed.

For the OEB Cost Assessment Variance Account, Union proposed to allocate the balance to rate classes in proportion to the 2013 OEB-approved administrative and general operating, maintenance and administration (OM&A) expenses.[26] OEB staff has previously argued that the balance in the account should not be recovered. However, if the OEB agrees with Union that the balance should be recovered, OEB staff believes that the proposed allocation methodology is appropriate as it is similar to how OEB cost assessments are included in rates.

For the Panhandle Reinforcement Project Costs Variance Account, the 2017 balance in the account reflects the actual net revenue requirement as there was no amount related to this project included in 2017 rates. Union proposed to allocate the balance to rate classes on the basis of an updated cost allocation study (using the OEB-approved 2013 study as a starting point), which includes the project costs and revenues associated with the project.[27] OEB staff believes that the proposed allocation methodology is appropriate as it is similar to that which is applied to Union's other major capital project accounts (the only difference for 2017 being that it is the entire net revenue requirement

[22] EB-2017-0091.
[23] EB-2011-0210.
[24] EB-2015-0181.
[25] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 3 / pp. 1-2.
[26] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 3 / p. 9.
[27] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 3 / p. 10.

amount being allocated as opposed to the variance between actual and OEB approved).

Disposition of 2017 Deferral and Variance Account Balances

For general service rate classes, Union proposes to dispose of the deferral and variance account balances prospectively over a 6-month period (January 1, 2019 – June 30, 2019).

For in-franchise contract and ex-franchise rate classes, Union proposes to dispose of the deferral and variance account balances as a one-time adjustment with the January 2019 bills customers receive in February 2019.[28]

OEB staff submits that the proposed approach is consistent with how Union has disposed of deferral account balances during the current IRM term as previously approved by the OEB. The only difference is that the balances are typically disposed over a 6-month period beginning October 1. Given the timing of the filing, that is not possible with respect to the 2017 balances.

Bill Impacts

If the application is approved as filed, the charge / credit for the 6-month period (January 1, 2019 – June 30, 2019) for a typical residential customer is as follows:

- Union South - $6.87 debit
- North East - $6.36 debit
- North West - $13.72 credit

If the OEB accepts OEB staff's arguments set out above, the bill impacts will change.

All of which is respectfully submitted.

[28] EB-2018-0105, Pre-filed Evidence, Exhibit A / Tab 3 / p. 11.