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July 3, 2019

Reply To: Thomas Brett
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Our File No. 185430

VIA RESS, EMAIL AND COURIER

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

Attention: Kirsten Walli
Board Secretary

Dear Ms. Walli:

Re: EB-2018-0305: Enbridge Gas Inc., Application for 2019 natural gas rates and other charges effective January 1, 2019

Please find enclosed herewith BOMA's Final Argument.

Yours truly,

FOGLER, RUBINOFF LLP

Tom Brett

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

EB-2018-0305

ONTARIO ENERGY BOARD

Enbridge Gas Inc.

2019 Rates Application

Final Argument of

Building Owners and Managers Association of Greater Toronto ("BOMA")

July 3, 2019

Tom Brett
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Counsel for BOMA

Final Argument of BOMA

Issue 1

Enbridge Gas Inc. ("Enbridge") did not respond appropriately to all relevant directives from the Merger proceeding. Please see BOMA's response to Issue 7(a) for a discussion of how Enbridge responded to the Board's findings and directives in that case.

Issue 2

Settled (see Settlement Agreement).

Issue 3

Settled (see Settlement Agreement).

Issue 4

Settled (see Settlement Agreement).

Issue 5

Partial Settlement (see Settlement Agreement.

Issue 6

Settled (see Settlement Agreement).

Issue 7

Partial Settlement (see Settlement Agreement).

Issue 7(a) – One-time Adjustment for Capital Pass-Through Projects

In EB-2017-0306 and EB-2017-0307 (the "Merger" case), the Board found:

> *"The OEB agrees with intervenors who noted that through Union Gas' capital pass-through, the mechanism, significant capital additions have been funded through rates during the past IRM term. The rate base and depreciation associated with projects that were found eligible for capital pass-through treatment during the IRM term shall be added to the 2013 OEB approved rate base and depreciation in determining the eligible incremental capital amount for Union Gas' service territory"* (p33).

The Board also noted that:

> *"...for EGD, the rate base and depreciation to be used in the formula shall be the OEB approved amount from the most recent custom IR update decision – EB-2017-0086"* (p33).

The two utilities were put on a comparable basis for purposes of calculating their ICM materiality thresholds, and the amount of eligible incremental capital for their respective service territories.

Enbridge complied with this direction. However, the applicant proposed to freeze the gradually declining revenue requirement generated by the six pass-through capital projects approved as Y-factors driving the previous 2014-2018 IRM term at the 2019 revenue requirement level for the duration of the 2019-2023 IRM plan and perhaps beyond. This proposal would increase the revenue requirement by approximately $46. 2 million over the proposed 2019-2023 IRM term alone (JT1.2), resulting in a substantial rate increase. The proposal results in a rate increase to offset the lower revenue requirement (and rates) that would have resulted from utilizing the higher ICM materiality threshold and, therefore, the lower incremental ICM eligible capital capacity, driven by the use of Board-directed rate base and depreciation additions to the Union 2013 rate base. The $46.2 million is the sum of the difference between the 2019 revenue requirement level and the revenue requirement level which results from the continuation of the gradual decline of depreciation, rate base, taxes, and return over the 2019-2023 deferred rebasing period.

BOMA opposes the proposed change in the Union rate zone rate design, for several reasons.

First, Enbridge's proposed "one-time true-up" is a major rate design change, resulting in a substantial rate increase, proposed at the midpoint of a ten year ICM period. The proposed rate change should not be considered in this proceeding.

In Procedural Order No. 2 in this proceeding, the Board stated that it was loath to deal with significant rate design changes in a mechanistic IRM case. It stated in Procedural Order No. 2:

> *"...this is an IRM application. Adjustments to rate design are generally not considered during an IRM term. To the extent that the rate design proposals are implementing the results of previous OEB decisions, or are required to transition to the OEB-approved IRM framework, the OEB will consider them. Otherwise, they should wait until the next rate rebasing application".*

The Board's reluctance to make any substantial rate design change during an IRM period was also reflected in its decision in Procedural Order No. 2 to change the wording of the rate design issue in the Issues List from:

> *"Are the rate design proposals for the Union Gas rate zones appropriate?"*

to:

> *"Are any rate design proposals appropriate in the context of previous OEB decisions, including ...".*

In BOMA's view, any such change should be dealt with at rebasing.

Moreover, the Board's extenuating factors, included in this paragraph from Procedural Order No. 2, reproduced above, do apply in this case. The true-up proposal does not implement the result of any prior OEB decision, including the Merger decision. To the contrary, the applicant's "true-up" proposal is designed to nullify the impact of the Board's directive to the applicant, with respect to amounts to be added to the 2013 Union rate base, for the purpose of determining the 2019 materiality threshold for ICM financed projects in the Union rate zone. Second, the Board made no direction to make the rate design change now proposed. To the contrary, the Board directed that the deferral accounts for the Union six pass-through projects in the 2014-2018 plan should remain open. Nor did the Board authorize that their scope be fundamentally changed to deal only with income tax timing differences. The Board stated that:

> *"The OEB accepts the applicants' proposal for the accounts that will be continued with the exception of the Cap and Trade deferral account and variance accounts which will be addressed in a separate proceeding"* (Merger, p46).

The Board approved the continuation of the accounts in the deferral rebasing period because they remain necessary to deal with variances between the forecast revenue requirement impacts of the six pass-through projects and the actual revenue requirement impacts thereof. The Board did not, as noted above, decide that the scope of the accounts be narrowed in the manner suggested by Enbridge in this application.

Moreover, the proposed rate design change is not required for Enbridge to transition to the OEB approved IRM framework for the deferral rebasing period. The existing price-cap IRM framework, chosen by Union for the 2014-2018 IRM program, simply continues for the five year deferred rebasing period, 2019-2023.

Second, the purpose of the ICM materiality threshold was to provide a tool for the Board to determine what amount of capital investment a utility would be expected to finance from rates during a five year price cap IRM program. The concept focuses on the utility's cash flow. "From rates" in this context means the combination of deprecation, revenue growth from new customers, and the Board approved annual price or revenue cap increase. The Board determined that the utility would have the ability to propose ICM financing to the extent that its proposed capital budget, including the ICM projects, exceeded its materiality threshold. However, the utility is not given a blank cheque with its capital budget. It is required to pace and prioritize its capital project spending. Furthermore, the Board anticipated that a utility would not normally "use up" all its "ICM capacity" with ICM projects, and suggested that utilities proposing several sizeable capital projects over a five year period should select a custom IR plan rather than a price cap IRM. While the custom IR option was not available to Enbridge during the deferred rebasing period, Enbridge was well aware of this fact, and decided to merge the companies nonetheless, because of the longer term benefits.

Furthermore, the applicants made it clear in their Final Argument in the Merger case that if the OEB issued a decision that made significant changes to the applicants' proposal, then the applicants would consider the plans for amalgamation in view of the decision (Merger, p55).

The Board decided to allow the merger, including a five year deferred rebasing period (EGD and Union, the merging corporations, both completed their previous IRM plans on December 31, 2018), and had asked the Board for a ten year deferred rebasing. The Board granted EGD a five year deferred rebasing. The Board also, as noted above, directed Union, for the purpose of calculating its materiality threshold under the ICM policy for the deferred rebasing period, to add to its 2013 rate base, the rate base and depreciation generated by the six projects awarded "pass-through" treatment over the 2013-2018 period. A few months after the Merger decision, the applicants advised the Board that they would proceed with the merger, and proceeded to complete the merger on January 1, 2019. The applicants were well aware that both the Merger decision and the Report of the Board on Ratemaking Associated with Distributor Consolidation, EB-2014-0138, issued March 26, 2015, directed that the IRM framework for the five year deferral rebasing period granted by the Board would, for each of the Union and EGD rate zones, be a price cap IRM and would also have been well aware of the implications of the Board's decision on the materiality threshold calculations for its two rate zones for 2020. In those circumstances, it is neither fair nor consistent with the Board's clearly stated policy for the Board to approve Enbridge's proposed major change in rate design during the deferral rebasing period, which is a proceeding which the Board has declared is, or should be, mechanistic in nature.

Third, Enbridge has a 2019-2023 capital budget of approximately \$2.5 billion. Over the previous IRM term, Enbridge actuals (2018 account forecast) capital budget was approximately \$3 billion, while Union's, notwithstanding its smaller size, spent about \$3.4 billion (2018 account forecast), resulting in rate bases for purposes of calculating the respective materiality thresholds of \$4.68 billion for EGD and \$3.72 billion for Union. Their materiality thresholds provide Enbridge with only \$13 million of ICM capacity in 2019, while Union has \$152 million of incremental capacity, more than ten times the EGD amount. Part of the reasons for Union's larger capacity is that its proposed capital budget for 2019 is approximately \$46 million larger than EGD's, which expands the capacity by that amount. Another reason is that for those capital expenditures in the 2014-2018 term, other than the six pass-through projects, Union proposes to use rate base numbers from 2013, not 2018 (Exhibit B1, Tab 2, Schedule 1, p10). Furthermore, Union used a 0.72% index to calculate the revenue available from the 2020 rate increase, which, in our view, understates that increased revenue that may be used to fund incremental projects.

The Board found that the:

> *"eligible incremental capital account will be determined using the OEB's ICM formula, and each gas utility's rate base and depreciation, ie. calculated separately for both Union Gas and Enbridge Gas".*

The Board's formula for calculating the eligible incremental capital amount, the potential space or capacity the utility would have in a given year to access the ICM funding mechanism is laid out in EB-2014-0219 and EB-2014-0202, as well as in the Chapter 3 Incentive Rate-Setting Application of the OEB's Filing Requirements for Electricity Distribution Rate Applications, July 20, 2017.

<u>Issue 8</u>

Settled (see Settlement Agreement).

<u>Issue 9</u>

BOMA does not agree that EGD's and Union's ISPS and AMPs support approval of the ICM funding request. Union is including low priority projects in its capital expenditure plans and budgets, to act as a buffer in the event unexpected projects require incremental funding. These, set aside, are substantial. There is a buffer, which is included in rates, which can be used to fund such projects.

As for EGD's rate zone, EGD's method of constructing its capital plans/budgets based on the requirements on an individual asset category basis, and its refusal to prioritize projects on an annual, or longer term basis diminishes its usefulness in supporting any particular ICM project.

Issue 10

BOMA is of the view that overheads should be part of capital costs, in order to provide the Board on a consistent basis and eligibility of projects for ICM funding. However, they should not be part of the revenue requirement calculation to the extent that they are already in rates.

ICM Projects – Introduction

In EB-2017-0306/EB-2017-0307, EGD/Union had requested Y-factor (pass-through) status for proposed investments over the plan term that qualify for ICM treatment. The Board did not approve this proposal. The Board acknowledged that the applicant might apply for ICM financing for qualifying capital projects over the five year extension of the 2014-2018 IRM to 2023. It stated:

> *"The distributor would therefore be able to identify projects for ACM or ICM treatment if its capital budget for the project year exceeds the Board's defined materiality threshold* [for that year]. *The materiality threshold is in effect a capital expenditure threshold which serves to demonstrate the level of capital expenditures that the distributor should be able to manage through its current rate".*

It found that such projects would be assessed, on a case by case basis, following the Board's current practice (Merger, p32, FN 45) to determine whether each capital project proposed for ICM financing met the current ICM criteria, and subject to a project specific materiality factor of $10 million (Merger, p33).

Issue 10 (Don River) and Issue 11

The Don River replacement project is the replacement of a pipeline crossing the Don River just north of Lake Ontario. Currently, the pipe is attached under a bridge over the Don River, and the proposal is to replace it with a pipeline under the river a short distance upstream of the bridge. The current pipeline is eighty-nine years old, and nearby construction activity will place it at risk. Enbridge is asking for an ICM of $13 million, the maximum amount possible under its 2019 ICM capacity. The total project cost is forecast at $35.3 million (EP.16, p2).

BOMA believes the project should not qualify for ICM financing. The replacement of a river crossing in-service for eighty-nine years is part of the normal year over year capital budget of the utility, and is part of the normal cycle of replacement and refurbishment of aged assets over time for the utility, and should have been planned and budgeted for in the normal course.

The utility has had many years to include the project in its annual capital budgets. Moreover, the amount requested is rather small, only $13 million, just $3 million above the project specific materiality factor of $10 million established in EB-2017-0306/EB-2017-0307 for the new combined utility. For perspective, Enbridge's forecast capital budget over the five year deferred rebasing period (2019-2023) is approximately $2.5 billion (Exhibit B1, Tab 2, Schedule 1, p4). Enbridge spent approximately $3 billion in its custom IR plan, which ended December 31, 2018. The $13 million, which occupies all of Enbridge's ICM "capacity" represents only one-half of one percent of the five year capital budget, and only about 2.5% of the 2019 capital budget. Such a small amount in relation to the capital budget should be absorbed by Enbridge without recourse to IRM funding.

Moreover, EGD rate zone Distribution System Plan does not offer any particular support to the project. In its plan, Enbridge has not prioritized its projects for 2019, and if the Don River crossing project is a high priority, it has not demonstrated that within its plan. A lower priority project could have been deferred. Moreover, Enbridge has indicated that it cannot give a numerical ranking to its 2019 capital projects. It considers its ten year list of projects all necessary at some point over the ten year period. Without such prioritization, BOMA cannot determine its ability to finance the entirety of the project (the $13 million requested) through the deferral of another project to a later year (1.BOMA.22, p2).

Finally, Enbridge has not stated what it will do if the ICM funding for the project is not approved in this case. BOMA assumes that construction has already commenced on the project in order to meet the December 2019 in-service date.

BOMA believes that the fact that a project, such as the Don River Replacement, has been determined to be in the public interest is not determinative of whether the project should receive ICM funding. The Board has been very clear on this point. It stated in Procedural Order No. 2 (p5):

> *"Determining that a project is in the public interest and determining whether it is eligible for incremental capital funding during an IRM term* <u>*have different considerations*</u>*. An ICM is a funding mechanism for significant, incremental and discrete capital projects for which a utility is* <u>*granted rate recovery in advance of its next rebasing application*</u>*. The OEB will use the established ICM criteria to determine whether the proposed ICM fits within the total eligible incremental capital amount, and that each project has a significant influence on the operation of Enbridge Gas. This will necessitate consideration of the proposed ICMs in the context of Enbridge Gas' overall USP and AMPs"* (our emphasis).

<u>Cost Increases for the Project</u>

The Board added Issue 10 to the Issues List. Issue 10 states:

> *"Are the costs of the ICM projects appropriate to the extent that they differ from the costs considered by the OEB in granting leave to construct".*

The Don River forecast project costs in this proceeding are $35.3 million, an increase over the $9.77 million over the costs forecast in the leave to construct on July 18, 2018 of $25.6 million, an increase of approximately 35% (I.EP.16, p2).

Enbridge has offered no substantial explanation for the increases in land costs or regulatory costs even though those items increased by 60% and 500%, respectively. In the absence of such evidence, the increase in land and regulatory costs of approximately \$2.1 million should not be allowed for reasons of prudency. They appear to be imprudent. In the leave to construct case (EB-2018-0108), the Board stated that the 30% contingency for the project was excessive. So, the effective overage was actually higher (p6).

The applicant failed to include overhead costs in its leave to construct proposals for Don River, Sudbury, Kingsville, and Stratford, all projects for which it is seeking ICM funding.

<u>Sudbury Replacement</u>

The Sudbury Replacement Project does not qualify for ICM treatment because the project was completed before December 31, 2019. The project came into service in October 2018 (Exhibit B1, Tab 2, Schedule 1, p24). Union has already spent the money to build the project during 2018 without applying for ICM assistance at that time. The purpose of the ICM policy is to allow utilities under price cap IRM to seek alternative funding and recovery in rates of projects that they feel are necessary and cannot be funded from rates. Allowing the completed project in one year to qualify for ICM treatment in a future year under IRM is contrary to Board's ICM policy, and would be a bad precedent. It would reduce the utilities' incentive to plan and pace its capital projects properly, to serve as a buffer for unexpected repairs or replacements. It would be a serious misuse of ICM. Second, there have been several replacement projects that required leave to construct in the same distribution system, and the company was well aware of the pipelines' condition.

Finally, Union claims that, notwithstanding that its capital expenditure over 2019 through 2023, Union is not able to reprioritize other projects. However, Union's evidence is that it includes low priority items in its annual budgets precisely to allow the flexibility to accommodate an unexpected requirement, like the Sudbury Replacement. (BOMA.22, p2) (our emphasis).

In the leave to construct application for the Sudbury project (EB-2017-0180), Union stated that the proposed pipeline replacement was a:

> *"continuation of three previous pipeline replacement projects in the Sudbury area"* (EB-2017-0180).

In BOMA's view, this suggests, even if the project were planned and constructed within the 2019-2023 IRM term, the project should be seen as part of the normal utility business periodic repair and replacement of older pipes, a key part of the year to year utility plants and budget, and therefore, not eligible for ICM funding.

In EB-2017-0180, the Board further noted that:

> *"The OEB is granting leave to construct the NPS 12 pipeline proposed by Union Gas, but has noted that Union Gas could improve future applications by providing the OEB with a forecast of growth to support the upsizing of any pipelines, as well as information on the longer-term plans for supply to an area in order to provide context for individual projects"* (our emphasis).

Union applied to the Board for leave to construct the Sudbury replacement project on May 6, 2017. However, Union had inspected the section of pipe in question in 2014-2015. The inspector noted substantial deterioration, and Union could have filed its application earlier, probably in 2016, but chose not to do so. Given that the pipeline section (which was the subject of the leave to construct replacement) was sixty years old, and the results of the earlier inspection, Union had ample reason to consider its replacement prior to 2017.

Costs

The actual cost of replacement of the pipeline was $95.2 million, up from $74 million in the leave to construct application, an increase of $21.2 million, or approximately thirty percent (I.EP.16, p3). Construction and labour costs increased by $8.9 million, over the original estimate of $58.361 million to $67.3 million. Overheads were not included in the leave to construct estimate, but added to the estimate in this proceeding at $12 million. The $95.2 million figure is inclusive of overheads.

Enbridge provided very little explanation for the $8.9 million increase in construction and labour costs.

Enbridge should not recover the additional $8.9 million in construction and labour, as the increase is of a magnitude that renders the additional costs imprudent.

Customer Consultation (All Four Capital Projects)

The cost consequences of the proposed large projects for which ICM funding is being sought, Kingsville, Sudbury, Don River, or Stratford, were not specifically put to customers during the consultation process (I.BOMA.79). They should have been. Most utilities proposing large discrete capital projects or programs, including Hydro One and Alectra, have put such projects, with their likely financial impacts, to customers to ascertain their willingness to pay higher rates to support them (I.BOMA.70).

Finally, in calculating the revenue impact of the Sudbury project offsets should be included for the $8 million to $10 million of capital projects would have otherwise had to have been spent during the deferral rebasing period (EB-2017-0180, p7).

<u>Kingsville Project</u>

The Kingsville Reinforcement Line project is proposed in response to increasing natural gas demand in the Kingsville-Leamington area. Much of the gas is required by the commercial greenhouse operators in the area. The Greenhouse Growers Gas Association noted that a December 2019 in-service date was necessary to maintain growth in the greenhouse gas sector. The proposed pipeline is a spur line off of the Panhandle system in the Town of Lakeshore, which will run south to the Kingsville/Leamington area, a region that contains the largest concentration of crops grown "under glass" in North America.

BOMA notes that while the Board found the Kingsville project to be in the public interest in EB-2018-0013, it also expressed a number of concerns with aspects of the project. The Board stated:

> *"While the OEB has approved the Project, there are some concerns that the OEB would like to observe.*
>
> *First, the new pipeline has ancillary distribution benefits according to Union in addition to the transmission functions. The distribution benefits are evident as Union identified 14 firm customer contracts executed and 20 customer contracts being negotiated which rely on the approval and construction of the Project. The OEB finds that the Project meets both distribution and transmission needs, yet the OEB's economic tests are exclusive, applicable to either distribution or transmission lines.*
>
> *Second, the economic test for transmission, E.B.O. 134, does not attribute who should pay with each stage of testing. For distribution pipelines, the more recent E.B.O. 188 test recognizes that if there is insufficient new revenue generated by the project to cover its costs, capital contributions are required from the benefiting parties. Under E.B.O. 134, the stage 2 benefiting parties would be downstream connecting customers and the local economy. Currently there is no mechanism to have these parties make a contribution to the costs despite their substantial benefit.*
>
> *For natural gas in Ontario, no economic test or ratemaking mechanism exists today to allow these discrepancies to be addressed.*
>
> *The OEB acknowledges the creative thinking included in IGUA's submission. While it is not appropriate to split the costing between transmission and distribution pipelines as*

> *proposed by IGUA in this proceeding, such proposals may help inform future thinking on the treatment of dual function pipelines"* (pp 5,6).

Given that the project is a blended transmission and distribution project, the deficiencies of the Board's "economic test for transmission", expressed above, the degree to which the project is supportive of the one particular sector, and given the Board's comments about IGUA's argument in the leave to construct proceeding for this project, BOMA urges the Board not to approve ICM funding for the Kingsville project. The project's timing has been moved up twice already, and it is highly likely that incremental revenues from the project will be high, both from the growers, and other users in the Leamington-Kingsville region, and the 0.45 pi is likely to understate the revenues from this line. The growers, a large and fast growing sector of the Ontario economy, were not asked to make contributions, and the fact that the construction of the project will eliminate the need of other expenditures, will provide an offsetting cash flow to the company. In reviewing the criteria of need and prudence in EB-2014-0219, the Board stated:

> *"Evidence that the incremental revenue requested will not be recovered through other means (e.g., it is not, <u>in full or in significant part, included in base rates or being funded by the expansion of service to include new customers and other load growth</u>)"* (our emphasis).

To summarize, EGD will recover substantial revenues from multiple sources to help finance the Kingsville project. It should not qualify for ICM funding. ICM funding for the Kingsville project would be an imprudent use of funds.

Finally, the project's cost increased from $105,716,000 in the leave to construct proceeding (EB-2018-0013) to $121.4 million in this proceeding. The forecast increase was due to the inclusion of overheads in the cost estimate. The applicant did not include overheads in the leave to construct application. Therefore, the cost was understated in that application by 15%.

Stratford Reinforcement Project

The applicant's evidence describes the project as a system service project, to increase the capacity of the Forest, Hensall-Goderich pipeline system to accommodate a gradually increasing load in the counties of Middlesex, Lambton Perth, and Huron. The project consists of 10.8 km of NPS 12 pipe at a cost of $28.5 million, projected to be in-service by the end of 2019. There is no change in forecast cost from that leave to construct estimate (EB-2018-0306). Union stated the project is required in late 2019 to serve additional customers in those counties. The project received leave to construct on March 28, 2019.

In any event, BOMA is of the view that the project is a routine increase in the capacity of Union's pipeline system to serve parts of four counties in southwestern Ontario. Many such lines are constructed over the life of a gas distribution company's existence, and they are a part of the normal cycle of continued improvements of service and meeting normal, gradual growth patterns in different parts of the franchise. As such, and given the relatively small size of the project, in relation to either the Union rate zone rate base or the EGD rate zone rate base, or the Enbridge gas corporate rate base, the project should not be considered eligible for ICM financial assistance.

BOMA also observes that Union has sought ICM treatment for $245.1 million in projects for 2019 alone, an amount well in excess of its eligible incremental capital capacity when calculated according to the Board's directive in the Merger case (EB-2017-0306 and EB-2017-0307). EGD's approach violates the Board's ACM/ICM policy. The Board has stated:

> *"The use of an ACM (ICM) is not appropriate for a distributor that ... is proposing to use the entire eligible incremental capital envelope available for a particular year".*

EGD is doing just that, and holds open the prospect of further ICM requests in the 2020, 2021, 2022, or 2023.

Issue 12

BOMA does not agree with EGD's proposal to use, for the calculation of the 2019 ICM threshold for the Union rate zone, the average of the annual PCI of Union and EGD rate zones since the last three rebasings which are 0.72% and 1.07%, respectively. EGD has submitted no evidence to support deviation from normal positions which is to use the EGD PCI of 1.07%.

Rate Riders

Finally, the credit balances from 2019 for the Don River (and Kingsville and Stratford projects) returned to ratepayers through a 2019 rate rider, which would reduce ratepayers' 2019 effective rates, should not be "netted" against the debit balance forecast for 2021 rates application. Ratepayers deserve to receive the credit in their 2019 rates. One cannot easily imagine Enbridge deferring (netting) its recovery of money owing in 2019 against a refund forecast for 2020. These credits and debits should be dealt with in the year incurred as a matter of fairness.

All of which is respectfully submitted.