Ontario Energy Board | Commission de l'énergie de l'Ontario

DECISION AND ORDER

EB-2020-0181

Enbridge Gas Inc. Phase 2 application for 2021 rates – Incremental Capital Module Funding Request

BEFORE: **Allison Duff**
Presiding Commissioner

Lynne Anderson
Chief Commissioner

Anthony Zlahtic
Commissioner

May 6, 2021

TABLE OF CONTENTS

1 OVERVIEW

This is a decision by the Ontario Energy Board (OEB) regarding an application filed by Enbridge Gas Inc. (Enbridge Gas) seeking approval for unit rates related to its 2021 Incremental Capital Module (ICM) funding request.

In a separate application, Enbridge Gas applied for rate changes related to its incentive rate-setting mechanism and other pass-through cost adjustments effective January 1, 2021 (Phase 1).[1] In a Decision and Interim Rate Order issued on November 6, 2020, the OEB accepted the settlement proposal between the intervenors and the applicant on all issues in Phase 1 of the proceeding. This is the second phase of the application that deals with just the ICM funding request related to two projects. If approved, the annual rate impact to fund the two ICM projects would be $2.71 for a typical residential customer in the Union South rate zone.

Enbridge Gas requested ICM funding for three capital projects which was later revised to two capital projects. For the reasons that follow, the OEB has made the following key determinations:

1. Enbridge Gas's request for ICM funding of $124.0 million for the London Line Replacement Project is approved.
2. Enbridge Gas's request for ICM funding for the Sarnia Industrial Line Reinforcement Project is not approved.
3. The ICM rate riders for the London Line Replacement Project will be based on the OEB-approved cost allocation methodology for the existing London Line.

[1] EB-2020-0095 (Phase 1)

2 THE PROCESS

On August 30, 2018, the OEB approved the amalgamation of Enbridge Gas Distribution Inc. (EGD) and Union Gas Limited (Union Gas) under the OEB's policy on mergers, amalgamations, acquisitions, and divestitures (MAADs). In its decision (the MAADs Decision), the OEB also approved a rate-setting framework and associated parameters for the deferred rebasing period of 2019 to 2023.[2] The companies amalgamated to form Enbridge Gas on January 1, 2019.

This application is the second phase of Enbridge Gas's request for rate changes in 2021. Enbridge Gas applied to the OEB on October 15, 2020, seeking approval for unit rates related to its 2021 ICM funding request. In its application, Enbridge Gas requested ICM funding for three capital projects which was later revised to two capital projects.

The OEB issued a Notice of Hearing on October 30, 2020. In Procedural Order No. 1, the OEB approved a list of intervenors, scheduled a discovery process and provided for filing of final arguments and reply by the applicant. In a letter dated January 28, 2021, Enbridge Gas requested that it be permitted to file updated evidence regarding the St. Laurent Phase 3 Replacement Project, a project for which Enbridge Gas requested ICM funding in this application. At around the same time, some intervenors filed letters with the OEB requesting a technical conference to seek further clarification regarding certain interrogatories.

In Procedural Order No. 3 issued on February 5, 2021, the OEB questioned Enbridge Gas's request to file updated evidence regarding the St. Laurent Phase 3 Project. The OEB expressed concerns regarding the delay in processing the application resulting from the filing of updated evidence, the regulatory overlap of examining the updated evidence in the current proceeding and a future leave to construct application, and the justification for reviewing the funding request for Phase 3 of the project in isolation as compared to the entire replacement project (Phases 3 and 4).

In a response dated February 10, 2021, Enbridge Gas withdrew its request seeking ICM funding for the St. Laurent Phase 3 Project. Enbridge Gas noted that it would request ICM funding for Phases 3 and 4 of the St. Laurent Project in a single ICM request within the 2022 rate application. Accordingly, Enbridge Gas confirmed that it was now requesting ICM funding for only two projects in this application: the London Line Replacement Project and the Sarnia Industrial Line Replacement Project.

[2] EB-2017-0306 / 0307

A technical conference was held on February 17, 2021. In Procedural Order No. 4 issued on February 19, 2021, the OEB scheduled a process for filing technical conference undertaking responses and final arguments. Enbridge Gas filed its undertaking responses on February 26, 2021 and its argument-in-chief on March 1, 2021.

Intervenors and OEB staff filed final arguments on March 12, 2021. The following intervenors filed submissions in this proceeding:

- Association of Power Producers of Ontario (APPrO)
- Building Owners and Managers Association (BOMA)
- Canadian Manufacturers and Exporters (CME)
- Energy Probe Research Foundation (Energy Probe)
- Environmental Defence
- Federation of Rental-housing Providers of Ontario (FRPO)
- Industrial Gas Users Association (IGUA)
- London Property Management Association (LPMA)
- Ontario Greenhouse Vegetable Growers (OGVG)
- Pollution Probe
- Quinte Manufacturers Association (QMA)
- School Energy Coalition (SEC)
- Vulnerable Energy Consumers Coalition (VECC)

Enbridge Gas filed its reply submission on March 23, 2021.

3 DECISION

3.1 Utility System Plan and Asset Management Plan

In accordance with the directions in the MAADs Decision, Enbridge Gas filed a consolidated Utility System Plan (USP) and Asset Management Plan (AMP) to support its 2021 ICM requests. The USP is a consolidated system plan for the amalgamated Enbridge Gas. The AMP reflects the asset plan for the next five years and explains the process to optimize the capital budget each year, with assets for the EGD and Union Gas rate zones being maintained separately for capital planning purposes through the end of 2025. The AMP outlines how Enbridge Gas plans, manages and develops the distribution, transmission and storage systems, and determines the capital investment requirement while balancing risk, performance and costs.

In Procedural Order No. 3, the OEB clarified the scope of the review of the USP and AMP for the purposes of this proceeding. The OEB noted that the review of the consolidated USP and AMP is necessary only so far as it provides context for hearing the ICM applications and determining the maximum eligible incremental capital for 2021.

3.1.1 2021 Capital Budget Forecasts

The USP includes Enbridge Gas's 2021 capital budget forecasts of $627.0 million for the Union Gas rate zones and $580.0 million for the EGD rate zone.

Some intervenors argued that Enbridge Gas had not justified its 2021 capital budget forecasts.

SEC submitted that in the absence of a complete review of the USP and AMP, the increase in the capital budget from 2020 to 2021 was not justified. SEC argued that Enbridge Gas was attempting to game the OEB's ICM guidelines and that its capital budget was developed on the premise that the utility is entitled to bring capital in-service up to the ICM materiality threshold without scrutiny of that spending. SEC further submitted that there was no evidence that Enbridge Gas made attempts to limit, optimize or defer certain spending in order to accommodate the ICM projects as part of its base capital budget.

FRPO submitted that the OEB needed a better understanding of asset condition, system renewal spending and the pacing of the investments in the USP to justify the proposition of the investments. FRPO expressed concern with the proposed increase in System Renewal spending. FRPO concluded that spending had almost doubled for the 2021 to 2025 period from the 2016 to 2019 period. FRPO argued that systems do not deteriorate to that extent in one year to require doubling of spending.

Environmental Defence suggested that any decision on the reasonableness of Enbridge Gas's 2021 capital budget forecast should be deferred until the next rebasing application.

LMPA submitted that the 2021 capital budget forecast should be reduced. In 2019, the OEB approved an in-service capital forecast of $518.5 million for the Union Gas rate zones yet the actual in-service addition was $507.8 million, a reduction of $10.7 million or approximately 2%. LPMA argued that this was a material reduction given the threshold to qualify for ICM funding was $10 million. Based on 2019, LPMA submitted that the OEB should reduce the 2021 in-service capital additions by a minimum of 2% or $12.5 million.

Energy Probe made a similar argument and calculated the change between the 2019 proposed in-service capital forecast and actual in-service capital to be $11.5 million, proposing a 2021 capital budget reduction of $11.5 million.

CME submitted that the 2021 capital budget forecast should be reduced by $10.7 million for the Union Gas rate zones as Enbridge Gas had not met its previous forecasts for in-service capital additions.

In reply, Enbridge Gas disagreed with SEC's and FRPO's assertions that its capital budget includes unreasonable increases and does not include rigorous prioritization and optimization. Enbridge Gas noted that the increases to System Renewal spending and the additional spending in the EGD rate zone had been explained in evidence. In the case of the Union Gas rate zones, Enbridge Gas submitted that the capital spend was supported by existing rates with the exception of the two ICM-eligible projects.

Enbridge Gas further noted that the 2021 initial capital budget for the Union Gas rate zones was $925 million and this was reduced to $627 million through the prioritization process. Enbridge Gas explained that it uses an iterative prioritization process to determine and optimize the budget. The "constraint" applied during the budget process is the ICM materiality threshold and it is only where the exercise fails (because projects that must be completed in the subject year exceed the threshold) that it seeks to further optimize by removing large ICM-eligible projects from the budget process to try to reduce the underlying budget further.

In response to intervenors' suggestions to reduce the 2021 capital budget, Enbridge Gas submitted that these intervenors were taking a selective view of spending for one year and drawing broad conclusions of the impact in future years. Enbridge Gas noted that modest variances in spending are inevitable. Enbridge Gas indicated that an under-spend of $10.2 million on a total forecast budget of $1,025.4 million is less than 1% of the total budget; this does not justify a reduction in the 2021 in-service capital addition forecast. In conclusion, Enbridge Gas submitted that it has provided appropriate and credible evidence to support its underlying 2021 capital budget for the Union Gas rate zones.

Findings

The OEB notes that Enbridge Gas has complied with the MAADs Decision in submitting a consolidated USP and AMP. The OEB finds that the USP and AMP, in addition to the Leave to Construct approvals for the London Lines Replacement and the Sarnia Industrial Reinforcement projects, provide sufficient information for the OEB to assess the 2021 ICM funding requests.

SEC, FRPO, Environmental Defence, LPMA, Energy Probe and CME submitted that Enbridge Gas's 2021 in-service capital forecast should be reduced or disallowed for a host of reasons.

As indicated in Procedural Order No. 3, this proceeding is part of an IRM application. The intent is not to undertake the same detailed assessment of the USP and AMP that would normally occur in a rebasing application (cost of service or Custom IR). The USP and AMP will be assessed in the next rebasing application, along with the overall capital plan.

The OEB is satisfied that Enbridge Gas has provided sufficient details of its consolidated capital plan and capital expenditures for the Union Gas rate zones to justify approving incremental funding in these current circumstances. However, as noted below, the USP and AMP should have included a proper year over year variance analysis, which was the subject of several interrogatories. Enbridge Gas's application also should have identified that the proposed 2021 in-service forecast capital included the harmonized capitalization policy.

The OEB's ACM Report requires:[3]

> If the forecasted total capital expenditures identified in a Price Cap IR application, are higher than what the distributor documented in its DSP in its previous cost of service application, the distributor needs to document the increases and the reasons for these.

While the last Union Gas cost of service application (prior to amalgamation) did not have a DSP/USP,[4] it is clear from the ACM Report that the OEB wants to assess the reasonableness of changes in capital expenditures. In future ICM funding applications,

[3] This requirement is in the EB-2014-0219 Report of the Board on New Policy Options for the Funding of Capital Investments: The Advanced Capital Module, dated September 18, 2014 (the ACM Report), p. 22.
[4] A USP is the natural gas version of a distribution system plan (DSP) that electricity distributors are required to file.

where there are year over year AMP increases in forecasted capital expenditures, the OEB expects Enbridge Gas to provide a variance analysis to explain the increase. This variance analysis is an important consideration in determining the reasonableness of the in-service capital forecast for the purpose of calculating the maximum eligible incremental capital. The purpose of the variance analysis together with the USP and AMP is to ensure that proper capital planning is done, and appropriate smoothing, prioritization and optimization of capital expenditures is being conducted to provide rate stability for customers. A review of the appropriateness of the 2021 in-service capital will be made at Enbridge Gas's next rebasing application.

3.1.2 Overheads in the 2021 Capital Budget Forecasts

The 2021 capital budget forecasts included overheads consistent with Enbridge Gas's post-amalgamation harmonized overhead capitalization policy. The harmonized overhead capitalization policy became effective January 1, 2020. Enbridge Gas did not provide a calculation of its 2021 capital budget forecasts based on the previous OEB-approved overhead capitalization policies for the EGD and Union Gas rate zones.

Enbridge Gas explained that due to its harmonized overhead capitalization policy, there has been an increase in the amount of overheads capitalized and a corresponding decrease in operation and maintenance (O&M) expenses, compared to legacy overhead capitalization policies. Enbridge Gas submitted that the Accounting Policy Changes Variance Account (Accounting Changes DVA), approved in the MAADs Decision, is capturing the revenue requirement of the reduction in O&M, net of the revenue requirement impact of the increase in capital. Enbridge Gas claimed that this account ensures that neither the utility nor the ratepayer benefits or is harmed.

Intervenors took issue with Enbridge Gas's application of its new overhead allocation policy for the purpose of determining is 2021 capital budget forecast.

LPMA submitted that the OEB should reduce the 2021 capital budget forecast as the new capitalization policy was not approved by the OEB. LPMA estimated the impact of the policy change to be $29.0 million. LPMA submitted that the 2021 capital budget for the Union Gas rate zones should be $585.6 million, reducing the $627.0 million proposed by Enbridge Gas by $29.0 million for overheads and $12.5 million for over-forecasting.

Energy Probe made a similar argument and calculated the impact of the change in accounting capitalization policy to be $47.6 million. Accordingly, Energy Probe submitted that the 2021 capital budget forecast for the Union Gas rate zones should be revised to $567.9 million, reducing the $627.0 million forecast by $47.6 million for overheads and $11.5 million for over-forecasting.

In reply, Enbridge Gas indicated that the total impact of the overhead capitalization policy change in 2020 for the Union Gas rate zones was an increase of approximately $8.0 million in capitalized expense, with a corresponding reduction to O&M expenses. Enbridge Gas argued that “it is fair to assume that the overall impact will not be substantially different in 2021”. Overall, Enbridge Gas forecast the 2021 change in overhead capitalization policy will result in increased capitalized overhead costs of $9.3 million.

Findings

Enbridge Gas has adopted a harmonized capitalization policy for the amalgamated utility, and this policy has yet to be approved for ratemaking purposes by the OEB. Current rates in the EGD and Union Gas rate zones are based on the pre-amalgamation capitalization policies.

The OEB finds the evidentiary record lacking because the impact of the overhead capitalization policy change on the 2021 capital budget has not been documented. Instead, estimates were provided in intervenor submissions and Enbridge Gas’s reply submission regarding the impact of the change in overhead capitalization policy.

With the withdrawal of the St. Laurent Replacement project from this ICM application, the maximum eligible incremental capital calculation for the EGD rate zone is not relevant. However, the 2021 capital budget forecast for the EGD rate zone informs the second ICM project-specific materiality test regarding the significance of the ICM funding requests to the overall utility.

For the Union Gas rate zones, the 2021 in-service capital forecast is used to derive the maximum eligible incremental capital which is part of the OEB’s eligibility for ICM funding calculations for the remaining two ICM funding requests. The OEB is concerned that Enbridge Gas’s 2021 in-service capital forecast is higher with the inclusion of overheads based on a capitalization accounting policy yet to be reviewed and approved by the OEB for ratemaking purposes.

In any future ICM application filed during the deferred rebasing period, the OEB requires Enbridge Gas to include the in-service capital forecast and ICM funding calculations based on both the previously approved and the new harmonized overhead capitalization policies.

The OEB’s findings on the maximum eligible incremental capital for the two ICM funding requests in the Union Gas rate zones are in the “Project-Specific Materiality” sections of this Decision.

3.2 Eligibility for ICM Funding

The ICM is a funding mechanism for significant, incremental and discrete capital projects for which a utility is granted rate recovery by means of rate riders in advance of the next rebasing application. To qualify for ICM funding, a request must satisfy the eligibility criteria of materiality, need and prudence, as set out in section 4.1.5 of the ACM Report. Changes to the materiality threshold were made in the Supplemental Report.[5]

In the MAADs Decision, the OEB permitted Enbridge Gas to request ICM funding during the deferred rebasing period. The OEB also determined that any individual project for which ICM funding is sought must have an in-service capital addition of at least $10.0 million, to reduce the chance that any proposed ICM project will be found not to be significant.[6] In the 2019 rates decision, the OEB outlined the approach that would be used to evaluate Enbridge Gas's ICM requests during the deferred rebasing term, including the manner in which the materiality threshold would be calculated.[7]

3.2.1 Need and Prudence

Enbridge Gas filed a Leave to Construct (LTC) application with the OEB for the Sarnia Industrial Line Reinforcement (Sarnia) Project on October 7, 2019.[8] The project is to install approximately 1.2 km of NPS 20 pipeline and ancillary facilities from the Dow Valve site to the Bluewater Interconnect including tie-ins to the existing Sarnia Industrial Line system. The project is needed to supply the increased demand for reliable and safe delivery of natural gas and future growth in the Sarnia area, specifically to support a $2 billion expansion of Nova Chemicals' existing Corunna site.

The OEB approved the Sarnia Industrial Line Reinforcement LTC application on March 12, 2020.[9] In its decision, the OEB addressed the need for the project and prudence of the capital expenditure.

Enbridge Gas filed a LTC application with the OEB for the London Line Replacement (London) Project on September 2, 2020.[10] The project involves replacement of the existing London Lines in their entirety. The existing London Lines are comprised of the London South Line and London Dominion Line which are two pipelines that are parallel to each other, approximately 60 km and 75 km in length, respectively. The proposed

[5] EB-2014-0219, New Policy Options for the Funding of Capital Investments: Supplemental Report, January 22, 2016, p. 19.
[6] EB-2017-0306/0307, Decision and Order, August 30, 2018, pp. 32-33.
[7] EB-2018-0305, Decision and Order, September 12, 2019, pp. 15-17.
[8] EB-2019-0218
[9] EB-2019-0218 Decision and Order, March 12, 2020, p. 1.
[10] EB-2020-0192.

project involves replacing the existing London Lines with approximately 90.5 km of NPS 4 and NPS 6 dual fed pipeline. In its LTC application, Enbridge Gas noted that the proposed pipeline is necessary to replace the existing pipeline due to integrity concerns.

The total forecast cost for the London project, including indirect overhead costs, is $161.1 million. Of this amount, $124.0 million is forecasted to go into service in 2021. Enbridge Gas submitted that the balance of the project cost is largely for abandonment costs that do not constitute in-service capital amounts for ICM eligibility purposes. The 2021 in-service amount filed in this application was $3.0 million lower than that filed in the LTC application. Enbridge Gas explained that the difference results from updated overhead costs allocated to the London project.

The OEB approved Enbridge Gas's London Line Replacement LTC application on January 28, 2021.[11] In its decision, the OEB addressed the need for the project and noted that it was prudent for the company to proceed with the project considering the age and deteriorating condition of the existing pipeline and that the projected costs were reasonable.[12]

The ICM policy further requires assessment of whether ICM funding is needed by meeting the following criteria:

- the Means Test
- the amounts must be based on discrete projects, and should be directly related to the claimed driver
- the amounts must be clearly outside of the base upon which the rates were derived[13]

Under the Means Test, if a distributor's regulated return on equity (ROE) exceeds 300 basis points above the deemed ROE embedded in the distributor's rates, then the funding for any incremental capital project is not permitted.[14] Enbridge Gas in its application confirmed that its ROE did not exceed 300 basis points above the deemed ROE. The actual 2019 ROE for Enbridge Gas was calculated to be 10.475% which is less than 300 basis points above the 2019 OEB-approved ROE of 8.98%.[15]

With the exception of FRPO, no party took issue with Enbridge Gas meeting the ICM funding criteria of need and prudence related to the London and Sarnia projects.

[11] EB-2020-0192.
[12] EB-2020-0192 Decision and Order, January 28, 2021, pp. 2 and 11.
[13] ACM Report, p. 17.
[14] Ibid, p. 15.
[15] EB-2020-0134, Enbridge Gas argument-in-chief, para 27.

Findings

The OEB finds that need and prudence were addressed in the LTC decisions for both the London and Sarnia projects and that Enbridge Gas passes the Means Test. The OEB also finds that the London and Sarnia projects are discrete projects, not part of a typical annual capital program, and the amount of funding is outside the base upon which rates were derived.

3.2.2 Materiality

There are two materiality tests related to ICM applications. The first test is the ICM materiality threshold formula, which serves to define the level of capital expenditures that a distributor should be able to manage within current rates. The test states that: "Any incremental capital amounts approved for recovery must fit within the total eligible incremental capital amount" and "must clearly have a significant influence on the operation of the distributor".[16] The second is a project-specific materiality test.

3.2.2.1 Materiality Threshold

Enbridge Gas calculated a 2021 materiality threshold value of $474.2 million for the Union Gas rate zones using the formula established by the OEB in its ICM policy. With the withdrawal of the St. Laurent project, the materiality threshold for the EGD rate zone is no longer relevant.

The ICM materiality threshold calculation includes the Price Cap Index (PCI), growth factor, rate base and depreciation amounts. Enbridge Gas used the current year PCI of 1.7%[17] in the ICM threshold capital calculation. The 2021 growth factor for the Union Gas rate zones has been calculated by comparing the percentage difference in annual revenues between 2019 (the most recent complete year) and 2013 (the last rebasing year) as the approved base year revenues.

The MAADs Decision determined that for the Union Gas rate zones, the materiality threshold would be based on the 2013 OEB-approved rate base and depreciation plus the 2019 forecast amount of rate base and depreciation associated with projects that were found eligible for capital pass-through treatment and included in Union Gas's base rates during the 2014 to 2018 IRM term.[18]

[16] ACM Report, p. 17.
[17] EB-2019-0194 Decision and Interim Rate Order, December 5, 2019.
[18] Exhibit B, Tab 2, Schedule 1, p. 12.

Findings

The OEB accepts Enbridge Gas's calculation of the materiality threshold value of $474.2 million for the Union Gas rates zones. The calculation adheres to the OEB's formula in the ACM Policy and the MAADs Decision.

3.2.2.2 Maximum Eligible Capital

The maximum eligible incremental capital determines the maximum ICM funding that a utility can request during a rate year and is based on the capital budget forecast. Based on its 2021 capital budget forecast for the Union Gas rate zone of $627.0 million, Enbridge Gas calculated the 2021 maximum eligible incremental capital available at $152.8 million. Both the London and Sarnia projects are in the Union South rate zone.

Table 1 summarizes the 2021 in-service capital amounts and the ICM funding request by project and in total. For the Sarnia project, although the 2021 in-service amount was $31.5 million, Enbridge Gas reduced its ICM funding request by $2.7 million to $28.8 million such that its total ICM funding request did not exceed the maximum eligible incremental capital for the Union South rate zone.

Table 1 – ICM Funding Calculations

	Union Gas Rate Zones ($ millions)
2021 In-Service Capital Budget Forecast	627.0
Less: Materiality Threshold Value	474.2
Maximum Eligible Incremental Capital	**152.8**
London Lines Replacement ICM Funding Request	124.0
Sarnia Industrial Reinforcement ICM Funding Request	28.8
Total ICM Funding Request	**152.8**

Some intervenors submitted that Enbridge Gas's 2021 capital budget forecast of $627.0 million and corresponding maximum eligible incremental amount of $152.8 million should be reduced for the Union Gas rate zones (see "2021 Capital Budget Forecasts" section of this Decision).

LPMA submitted that Enbridge Gas's 2021 maximum eligible incremental capital amount should be reduced from $152.8 million to $111.3 million for the Union Gas rate zones. Energy Probe submitted that the 2021 maximum eligible incremental capital should be reduced from $152.8 million to $93.7 million for the Union Gas rate zones.

In reply, Enbridge Gas argued that the revenue requirement impact of the change in overhead allocations in the Union Gas rate zones will yield a net credit to ratepayers, which will be recorded in the Accounting Changes DVA. Enbridge Gas claimed that ratepayers will be kept whole through the Accounting Changes DVA. If an adjustment was made to the maximum eligible incremental amount to account for the capitalization policy change, then the same change would be reflected twice, "which would amount to double counting".

Findings

The OEB finds that Enbridge Gas accurately calculated the maximum eligible incremental capital at $152.8 million for the Union Gas rate zones based on its harmonized overhead allocation and 2021 capital budget forecast. The OEB addresses the maximum eligible incremental capital issue further in the "Project-Specific Materiality" section 3.2.2.3 of this Decision.

3.2.2.3 Project-Specific Materiality

The OEB adopted a second, project-specific materiality test in the ACM Report. The project-specific materiality test is as follows:

> Minor expenditures in comparison to the overall capital budget should be considered ineligible for ACM or ICM treatment. A certain degree of project expenditure over and above the Board-defined threshold calculation is expected to be absorbed within the total capital budget.[19]

<u>Sarnia Industrial Line Reinforcement: Project-Specific Materiality</u>

Enbridge Gas requested ICM funding of $28.8 million for the Sarnia project. Although the capital budget was higher, Enbridge Gas reduced its ICM funding request to not exceed its calculated 2021 maximum eligible incremental capital for the Union Gas rate zones (see Table 1). Enbridge Gas confirmed that the balance of the 2021 Sarnia project costs would be accommodated within the ICM threshold.[20]

In this application, Enbridge Gas increased the capital budget for the Sarnia project to $32.9 million from the original estimate of $30.8 million in its LTC application. Enbridge Gas indicated that the variance was due to a change in overhead allocations and the 2021 in-service costs were $31.5 million.

APPrO, QMA and OEB staff supported ICM funding for the Sarnia project. Other intervenors who made submissions on the issue opposed ICM funding.

[19] ACM Report, p. 17.
[20] Enbridge Gas argument-in-chief, March 1, 2021, para 44.

Energy Probe, LPMA and OGVG submitted that the project should not be approved for ICM funding as the project would generate sufficient revenue. These intervenors argued that if approved for ICM funding, the revenue requirement would be $3.9 million over the 2021 to 2023 deferred rebasing period, yet the project would generate an estimated incremental revenue of $5.8 million over the same period.[21]

The consideration of incremental revenue generated by an ICM funded project was addressed by the OEB in Enbridge Gas's 2019 ICM funding request (2019 Rates Decision) for the Kingsville Transmission Reinforcement (Kingsville) project. In the 2019 Rates Decision, the OEB found it appropriate not to include incremental revenues in determining the maximum eligible incremental capital for ICM eligibility.[22] In its decision, the OEB stated:

> The OEB notes that the ICM policy does not require utilities to record possible incremental revenues in a deferral account or include it in the rate rider. As discussed under section 4.3.2, the ICM policy is being applied to the current framework, and the policy should apply in its entirety. The materiality threshold calculation for determining the maximum eligible incremental capital includes a growth factor that accounts for incremental revenues and growth in customers that may arise due to the implementation of an ICM eligible project. The OEB further notes that Enbridge Gas is under a Price Cap IR wherein revenues and costs are decoupled.[23]

Several intervenors argued that the Sarnia project is expected to generate surplus revenue during the deferred rebasing term, which was fundamentally different from the Kingsville project. As the incremental revenue generated by the project is more than adequate to cover its revenue requirement, the OEB should reject Enbridge Gas's request for ICM funding for the Sarnia project. BOMA, FRPO, Pollution Probe, SEC and VECC supported these submissions.

LPMA and OGVG submitted that Enbridge Gas, in not considering incremental revenue, was misconstruing the evidence and submissions in the 2019 rates proceeding. For the Kingsville project, Enbridge Gas requested $36.9 million in revenue requirement and forecast incremental revenues of $7.0 million, resulting in a revenue shortfall of $29.9 million and the need for ICM funding.

[21] OEB Staff IRR# 4(c) and OGVG IRR# 1.
[22] EB-2018-0305 Decision and Order.
[23] EB-2018-0305 Decision and Order, September 12, 2019, p. 26.

OEB staff disagreed. OEB staff submitted that based on the determination of the OEB in the 2019 Rates Decision, incremental revenues generated from the Sarnia project do not require inclusion in the calculation of the revenue requirement.

Some intervenors referenced the OEB's Chapter 3 filing requirements, that a request for incremental capital during the IRM term should include evidence that the revenue requested will not be recovered through other means. SEC submitted that Enbridge Gas had not complied with the filing requirements since it did not disclose to the OEB that the incremental revenues from the project are expected to exceed the revenue requirement of the capital spend.

VECC submitted that the Sarnia project was not material in comparison to the overall capital budget of the amalgamated utility and should be classified as "business as usual".

In reply, Enbridge Gas argued that under the OEB's ICM policy, surplus incremental revenue is not determinative of the need for ICM treatment. Enbridge Gas referred to the 2019 Rates Decision[24] wherein the OEB recognized that Enbridge Gas was under an IRM where revenues are decoupled from costs. Enbridge Gas interpreted this to mean that whether a particular project on its own is revenue positive or revenue negative does not dictate whether it is eligible for ICM treatment.

Enbridge Gas reiterated the OEB's findings for the Kingsville project. Enbridge Gas added that the annualized growth factor accounts for the drivers of revenue growth over time (i.e. growth in customers, volumes and contract demand) in the ICM materiality threshold calculation.

Enbridge Gas further argued that the Kingsville and Sarnia projects were not fundamentally different. Enbridge Gas submitted that the same principle, which is that incremental revenues are captured in the growth factor, should apply to the Sarnia project. In conclusion, Enbridge Gas submitted that the OEB should approve ICM funding for the portion of the Sarnia project that is not notionally funded by existing rates.

Findings

The OEB denies ICM funding for the Sarnia project. The OEB finds that the Sarnia project fails the project-specific materiality test as it is not significant in the context of the overall utility. In assessing significance, the OEB has considered the $5.8 million expected incremental revenue relative to the $3.9 million requested revenue

[24] EB-2018-0305 Decision and Order, September 12, 2019.

requirement over the 2021 to 2023 deferred rebasing period, and the $1.207 billion 2021 capital budget forecast for Enbridge Gas.

The ACM Report lists the evidence the OEB expects that a distributor provide to support the need for ICM funding, including:[25]

> Evidence that the incremental revenue requested will not be recovered through other means (e.g., it is not, 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).

The materiality threshold calculation includes a growth factor and there is no inclusion of incremental revenues in the formula. The Sarnia project cost exceeds that materiality threshold. Yet there are two materiality tests for ICM funding. The second test considers project-specific materiality in the context of the overall capital budget. In addition, despite the Sarnia project capital costs exceeding the $10 million minimum indicated in the MAADs Decision, the test of significance must consider incremental revenues generated.

The OEB finds that the evidence regarding the Kingsville project was distinctly different from the evidence regarding the Sarnia project. Given these differences, the OEB's decision regarding the Kingsville project does not limit consideration of incremental revenues for the Sarnia project. Unlike the Kingsville project with a revenue shortfall, the Sarnia project is expected to have a revenue surplus. Furthermore, the OEB concludes that the decision for the Kingsville project was about whether incremental revenue should be included in the materiality threshold calculation, a separate deferral account or in the ICM rate rider. It was not addressing whether the Kingsville project would have a significant influence on the operation of the utility. The OEB finds the Sarnia project does not qualify for ICM funding as it does not have a significant influence on the operation of the utility.

The OEB notes that Enbridge Gas's application did not indicate that the project was forecast to generate $5.8 million of incremental revenue. This evidence was adduced through intervenor interrogatories. Enbridge Gas's application was lacking in this regard. In the interest of efficiency, forecast incremental revenues should be included in all ICM funding requests.

[25] ACM Report, p. 25.

<u>London Lines Reinforcement: Project-Specific Materiality</u>

Enbridge Gas requested ICM funding of $124.0 million for the London project. Although the forecast total project cost, including indirect overhead costs, was $161.1 million, the 2021 in-service costs were $124.0 million. Enbridge Gas submitted that the cost balance was largely for abandonment costs that did not constitute in-service capital amounts for ICM eligibility purposes. The $124.0 million in-service cost in this application is $3.0 million lower than that filed in the LTC application. Enbridge Gas explained that the difference results from updated overhead costs allocated to the London project.

APPrO, BOMA, Energy Probe, LPMA, OGVG, Pollution Probe, QMA, VECC and OEB staff submitted that Enbridge Gas had met the ICM requirements and the project should be approved for ICM funding. However, many of these intervenors argued that the amount of ICM funding for the London project should be reduced or recalculated, based on the previous OEB-approved overhead capitalization policy for the Union Gas rate zones.

Energy Probe and LPMA made specific recommendations on reducing ICM funding for the London project below the $124.0 million requested by Enbridge Gas. Energy Probe submitted that the appropriate amount of ICM funding was $89.0 million. Energy Probe argued that the London project consisted of three discrete projects (London pipelines, Strathroy lateral and Strathroy gate station) and was not a single project for ICM purposes. Energy Probe submitted that the $124.0 million ICM funding request should be reduced by $27.2 million for allocated indirect overheads and $7.8 million for the Strathroy lateral pipeline and gate station. LPMA submitted that the maximum eligible incremental capital amount for the Union Gas rate zones should be reduced to $111.3 million due to an overstated 2021 capital budget, and ICM funding for the London project should not exceed that maximum.

Many intervenors were concerned that the Accounting Changes DVA would not protect ratepayers from over-collection of O&M expenses, if included in capitalized overheads and recovered in ICM rate riders.

CME, Energy Probe, LPMA and OGVG submitted that it was not clear how or if the Accounting Changes DVA captures higher ICM rate rider revenue as a result of the change in capitalization policy. They argued that the Accounting Changes DVA was not designed to deal with ICM applications and the impact of the new overhead capitalization policy. Unless Enbridge Gas could demonstrate that the account appropriately captures the impact of the new capitalization policy on ICM funding and the associated revenues generated through the rate riders, the overheads should be calculated in accordance with the previous OEB-approved capitalization policy.

Alternatively, LPMA suggested the establishment of a new ICM account in addition to the Accounting Changes DVA to ensure that neither the company nor ratepayers were harmed.

CME, Environmental Defence, FRPO and SEC submitted that the London project should not be approved for ICM funding. Specifically, Environment Defence took issue with the underlying need for the London project, given integrated resource planning, alternatives and the capital budget forecasts. FRPO submitted that the London project did not qualify as a high-risk priority project and was not prudent. SEC submitted that the OEB should “place a pause” on all incremental capital spending requests from Enbridge Gas, until such time as the OEB can consider the USP, AMP, future capital needs and the overhead allocation policy of the amalgamated utility at rebasing.

In reply, Enbridge Gas reiterated that the revenue requirement impact of the change in overhead capitalization policy, including impacts relevant to ICM projects, will be recorded in the Accounting Changes DVA and no further adjustments were required. Enbridge Gas further reiterated that the OEB in the past two rate proceedings[26] considered similar arguments and determined that indirect overheads are appropriately included in the ICM funding request.

Enbridge Gas maintained that the Strathroy lateral and Strathroy Gate Station are all part of the overall project. The London project is a single project with several inter-related components. Enbridge Gas noted that it presented the entire cost ($164.1 million) in the LTC application and it is appropriately seeking ICM treatment for the $124.0 million portion of the total cost that is forecasted to go into service in 2021.

Enbridge Gas disagreed with FRPO’s contention. Enbridge Gas submitted that the OEB already considered the need and prudence of the project in the LTC and FRPO was an active participant in that proceeding. The OEB in the LTC decision found that Enbridge Gas had demonstrated the need for the project and the estimated costs were reasonable.

Enbridge Gas also referred to the MAADs Decision where the OEB noted that, “During the deferred rebasing period, the applicants expect to change accounting policies and practices as part of the implementation of an integrated accounting system, including changes in the calculation of depreciation rates and its cost capitalization policy”.[27] In recognition of the fact that there could be impacts arising from changes in accounting policies, the MAADs Decision directed the establishment of the Accounting Changes DVA.

[26] EB-2018-0305 and EB-2019-0194.
[27] EB-2007-0306/0307 Decision and Order, August 30, 2018, p. 46.

Further, Enbridge Gas submitted that a portion of O&M costs are recovered as capitalized overheads and there is no double recovery. Enbridge Gas submitted that its O&M budget in cost of service filings always included offsets that recognize O&M amounts being capitalized.

Enbridge Gas submitted that ratepayers are protected from the impacts of unapproved accounting policy changes during the deferred rebasing period, because the revenue requirement impacts are recorded in the Accounting Changes DVA for later disposition.

Enbridge Gas in its reply submission stated that the impact of the change to overhead capitalized costs allocated was $8 million for 2020 and estimated to be $9.3 million for 2021.

Findings

The OEB approves ICM funding of $124.0 million for the London project, as proposed by Enbridge Gas, which includes application of the new, harmonized overhead capitalization policy. In approving $124.0 million, the OEB is not approving Enbridge Gas's new overhead capitalization policy as a comprehensive review will take place at rebasing.

This proceeding is unique as Enbridge Gas's harmonized accounting policy has affected the 2021 capital budget forecasts, the maximum eligible incremental capital amounts and the ICM project funding requests. Enbridge Gas's rebasing application will address many issues for review by stakeholders and the OEB. The entries and balances in the Accounting Changes DVA, approved in the MAADs Decision, will be reviewed at rebasing along with other accounting changes due to the amalgamation. At this time, the OEB expects that Enbridge Gas is making the appropriate entries to that account such that the utility and ratepayers neither benefit nor lose from an accounting policy change introduced during the deferred rebasing period.

The OEB concludes that the rebasing proceeding is the appropriate time to review the harmonized overhead capitalization policy, and the implications on O&M and capital during the deferred rebasing term. The onus will be on Enbridge Gas to demonstrate there has been no "double counting" or over-recovery of O&M through capitalized overheads recovered in approved ICM rate riders during the deferred rebasing period.

At rebasing, the OEB will be in a position to determine if the $124.0 million approved for ICM funding for the London project is materially different from the actual capitalized amount, net of accumulated depreciation. If materially different, the OEB may approve rate riders to "true-up" the difference between the approved $124.0 million and the actual capital costs, including capitalized overheads.

The OEB is not revisiting previous decisions regarding the inclusion of overheads, direct and indirect overheads, in ICM funding requests. The OEB approved the inclusion of indirect overheads in Enbridge Gas's ICM funding applications in 2019 and 2020 and is doing so for 2021 as well. To the extent that there is a material difference between the capitalized overheads used for the ICM funding and the final approved capitalized overheads for the London project, this can be considered in the determination of whether an ICM "true-up" is required.

Enbridge Gas explained that the harmonized overhead capitalization policy has resulted in an increase in the amount of overheads capitalized and a corresponding decrease to O&M expenses, compared to previous overhead capitalization policies. Until the harmonized policy is reviewed and approved for ratemaking, several intervenors submitted that the previous OEB-approved capitalization policies for the EGD and Union Gas rate zones should be applied to capital budgets and ICM funding requests. The increase in harmonized overheads capitalized increased the maximum eligible incremental capital available for ICM funding.

The OEB acknowledges this concern. As previously indicated in this Decision, the OEB requires Enbridge Gas to include capital budget and ICM funding calculations based on both the previously OEB-approved and the new harmonized overhead capitalization policies in any future ICM application filed during the deferred rebasing period. The two maximum eligible incremental capital calculations, for each of the EGD and Union Gas rate zones, can inform the OEB's consideration of the ICM funding requests.

In this proceeding, the OEB does not have sufficient information to recalculate the maximum eligible incremental capital for the Union Gas rate zones. Despite this lack of detail, the OEB finds it appropriate to approve $124.0 million in ICM funding for the London project. The project is $28.7 million less than the $152.8 million maximum eligible incremental capital amount calculated by Enbridge Gas that includes the amount associated with the harmonized overhead allocation. In approving the $124.0 million in ICM funding for the London project, the OEB has considered the potential maximum eligible incremental capital without harmonized overheads. The OEB concludes that there is limited risk that the maximum eligible incremental capital has been materially exceeded.

Cost Allocation for Approved ICM Funding

Enbridge Gas proposed to change the cost allocation methodology for the London project. The current cost allocation, approved in the last 2013 rebasing decision for the Union Gas rate classes, classifies the existing London Line as “Other Transmission” and allocates costs to Union South rate classes in proportion to the forecast firm design day demands.

Enbridge Gas proposed to change the current cost allocation in deriving ICM rate riders for the London project. Enbridge Gas proposed to classify the London project as a distribution asset and allocate it to rate classes in proportion to forecast Union South in-franchise design day demands of firm and interruptible customers served by the distribution system, excluding customers served directly off transmission lines. Enbridge Gas indicated that the proposed cost allocation was consistent with the plant accounting record categorization and the treatment of the Windsor Line Replacement ICM project approved by the OEB in Enbridge Gas’s 2020 rate decision.[28]

LPMA and VECC submitted that the proposed change would shift significant costs between the rate classes. LPMA noted that under the proposed methodology, the small general service rate classes in the Union South rate zone (M1 and M2) would see an increase in their allocated costs of more than $1.3 million. VECC argued that ICM proceedings are not the best forum for making changes to cost allocations. Accordingly, LPMA and VECC submitted that such a significant change should be considered as part of a comprehensive rebasing application where all changes including rate harmonization can be reviewed.

In reply, Enbridge Gas reiterated that classifying the London project as a distribution asset and the proposed cost allocation treatment was consistent with the Windsor Line Replacement Project. Enbridge Gas maintained that its proposed approach was appropriate in recognition of the character and purpose of the new line. Enbridge Gas further noted that intervenors will be able to revisit cost allocation issues at rebasing.

Findings

The OEB denies Enbridge Gas’s proposed cost allocation for recovering the approved ICM funding amount for the London project. The OEB finds it inappropriate to make a change of this magnitude as part of an ICM funding application.

The OEB directs Enbridge Gas to apply the approved cost allocation methodology embedded in current rates for the London project, consistent with cost allocation of the existing London Line facilities.

[28] EB-2019-0194

The London project is a replacement for existing facilities currently classified as other transmission for rate making purposes. The OEB finds it inappropriate to re-classifying an asset upon replacement during a deferred rebasing term.

Further, as found in prior rate proceedings, rate stability and predictability for customers during the deferred rebasing period prior to rebasing is a desired outcome of incentive rate regulation. At rebasing, there will likely be cost allocation changes, adjustments to rate base, possible rate harmonization and rate design proposals. Cost allocation issues as a whole will be examined in Enbridge Gas's next rebasing application.

4 IMPLEMENTATION

In a Decision and Interim Rate Order issued on November 6, 2020, the OEB implemented interim rates effective January 1, 2021 that reflected the IRM related adjustments.[29] The Interim Rate Order is effective until the OEB issues a final Rate Order in this proceeding.

ICM unit rates resulting from this Decision will be effective and implemented with the July 1, 2021 Quarterly Rate Adjustment Mechanism application. The London project is expected to go into service at the end of 2021, and therefore the OEB concludes that it is reasonable to commence the funding mid-year 2021, rather than providing funding for a full year.

Enbridge Gas is directed to file the ICM unit rates in a draft rate order to be effective from July 1, 2021 for the duration of the deferred rebasing period to recover the total revenue requirement for the London project from 2021 to 2023. The ICM unit rates shall also be based on the OEB-approved cost allocation methodology. The ICM unit rates will be embedded in the delivery and transportation charges on the applicable rate schedules and customer bills.

[29] EB-2020-0095

5 ORDER

THE ONTARIO ENERGY BOARD ORDERS THAT:

1. Enbridge Gas shall file with the OEB and forward to all intervenors a draft rate order attaching a proposed Tariff of Rates and Charges reflecting the OEB's findings in this Decision and Order, by **May 18, 2021**. The draft rate order shall include customer rate impacts and supporting information showing the calculation of the ICM unit rates.

2. Intervenors and OEB staff shall file any comments on the draft rate order with the OEB and forward them to Enbridge Gas on or before **May 25, 2021**.

3. Enbridge Gas shall file with the OEB and forward to the intervenors responses to any comments on its draft rate order on or before **May 31, 2021.**

4. Cost eligible intervenors shall file their cost claims with the OEB and forward them to Enbridge Gas on or before **June 14, 2021**.

5. Enbridge Gas shall file with the OEB and forward to the intervenors any objections to the claimed costs by **June 21, 2021**.

6. Intervenors shall file with the OEB and forward to Enbridge Gas any responses to any objections for cost claims by **June 28, 2021**.

7. Enbridge Gas shall pay the OEB's costs of and incidental to this proceeding upon receipt of the OEB's invoice.

How to File Materials

Parties are responsible for ensuring that any documents they file with the OEB, such as applicant and intervenor evidence, interrogatories and responses to interrogatories or any other type of document, **do not include personal information** (as that phrase is defined in the *Freedom of Information and Protection of Privacy Act*), unless filed in accordance with rule 9A of the OEB's *Rules of Practice and Procedure*.

Please quote file number, **EB-2020-0181**, for all materials filed and submit them in searchable/unrestricted PDF format with a digital signature through the OEB's web portal at https://p-pes.ontarioenergyboard.ca/PivotalUX/.

- Filings should clearly state the sender's name, postal address, telephone number, fax number and e-mail address.
- Please use the document naming conventions and document submission standards outlined in the Regulatory Electronic Submission System (RESS) Document Guidelines found at www.oeb.ca/industry.
- Parties are encouraged to use RESS. Those who have not yet set up an account, or require assistance using the web portal can contact registrar@oeb.ca for assistance.

All communications should be directed to the attention of the Registrar at the address below and be received by end of business on the required date.

With respect to distribution lists for all electronic correspondence and materials related to this proceeding, parties must include the Case Manager, Khalil Viraney at Khalil.Viraney@oeb.ca and OEB Counsel, Ian Richler at Ian.Richler@oeb.ca.

Email: registrar@oeb.ca
Tel: 1-877-632-2727 (Toll free)

DATED at Toronto, May 6, 2021

ONTARIO ENERGY BOARD

Original Signed By

Christine E. Long
Registrar