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Sent by EMAIL, RESS e-filing

Nancy Marconi
Registrar
Ontario Energy Board
2300 Yonge Street, Suite 2700
Toronto, ON M4P 1E4

Dear Nancy Marconi:

Re: EPCOR Natural Gas Limited Partnership ("EPCOR")
Ontario Energy Board ("OEB") File No. EB-2022-0184, Phase 2
Customer Volume Variance Account (CVVA)
Argument in Chief

In accordance with the OEB's Procedural Order No. 4, dated December 8, 2022, EPCOR's Argument in Chief for this proceeding is enclosed with this letter.

Should you have any questions, please contact the undersigned.

Sincerely,

T. H

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cc: Richard King, Osler, Hoskin & Harcourt LLP
Michael Millar, OEB Counsel
Arturo Lau, OEB Case Manager
Intervenors (EB-2022-0184, Phase 2)

ONTARIO ENERGY BOARD

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

AND IN THE MATTER OF an Application by EPCOR Natural Gas Limited Partnership pursuant to section 36(1) of the OEB Act for an order or orders approving or fixing just and reasonable rates and other charges for the sale and distribution of gas to be effective January 1, 2023 for the EPCOR Natural Gas Limited Partnership gas distribution system to serve the Municipality of Arran-Elderslie, the Municipality of Kincardine and the Township of Huron-Kinloss.

EPCOR NATURAL GAS LIMITED PARTNERSHIP

ARGUMENT IN CHIEF

EB-2022-0184 - PHASE 2 - CUSTOMER VOLUME VARIANCE ACCOUNT

A. INTRODUCTION

1. On July 18, 2022, EPCOR Natural Gas Limited Partnership (EPCOR) filed an incentive rate-setting mechanism application (the Application) with the Ontario Energy Board (OEB), in which it sought an Order for, among other things, approval to establish a new Customer Volume Variance Account (CVVA), including approval to record costs in the proposed account from January 1, 2020 until December 31, 2028.

2. On September 20, 2022, following the conclusion of written interrogatories, OEB staff filed a letter indicating that EPCOR's proposed CVVA was a material issue that would require additional time to evaluate. OEB staff therefore recommended that the Application be bifurcated into two phases, wherein Phase 2 would exclusively address the CVVA issue. EPCOR did not object to this proposal.

3. On September 27, 2022, the OEB issued Procedural Order No. 2, which bifurcated the Application and granted intervenor status to all OEB-approved intervenors in EPCOR South Bruce's 2019-2028 Custom IR proceeding, for Phase 2 of the current proceeding. The OEB also made provision for interrogatories and a settlement conference for Phase 2.

4. On October 27, 2022, EPCOR and the intervenors (School Energy Coalition and Vulnerable Energy Consumers Coalition) convened for a Settlement Conference regarding the CVVA. The parties were unable to reach a settlement agreement.

5. On October 18, 2022, EPCOR with support from the intervenors, filed a letter with the OEB recommending the next steps for the proceeding which included EPCOR filing additional evidence (to clarify and provide a step by step explanation of the mathematical formula used to calculate amounts recoverable under the CVVA and to identify financial impacts to the utility should the CVVA not be approved), interrogatories on the additional evidence, and a potential technical conference if determined by the parties to be beneficial.

6. On November 7, 2022, the OEB issued Procedural Order No. 3, which established a schedule for the procedural steps recommended by EPCOR as well as dates for the written hearing of this matter.

B. EXECUTIVE SUMMARY

7. The purpose of the CVVA is to allow EPCOR to record utility revenue shortfalls due to the variance between forecasted customer volumes and actual volumes for Rates 1 and 6 customers in its South Bruce operations.

8. EPCOR submits that the CVVA should apply to all Rate 1 and 6 customers who are subject to South Bruce rates (including Rate 1 and 6 customers served by new expansion projects where South Bruce rates apply) and that it should be permitted to record costs in the proposed variance account from January 1, 2021 until December 31, 2028.[1]

9. As outlined in the Application[2], the proposed CVVA meets the OEB's criteria of causation, materiality, and prudence for establishing a new variance account per the Board's Filing Requirements for Natural Gas Rate Applications.

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[1] In the Application, EPCOR had requested the ability to record costs in the CVVA effective January 1, 2020. However, in EPCOR's response to OEB Staff 4 (a) filed December 5, 2022 at p.8, the utility clarified that EPCOR is proposing an effective date for the CVVA of January 1, 2021.

[2] ENGLP Southern Bruce – 2023 IRM Application, filed July 18, 2022 at pages 35-36.

10. Moreover, approval of the CVVA is consistent with and upholds the ten-year regulatory compact that was central to the competitive process under which EPCOR was awarded a Certificate of Public Convenience and Necessity (CPCN) to construct the South Bruce gas distribution system and the subsequent ten-year custom incentive rate tariff. To deviate from this ten year deal would not only be in breach of prior regulatory approvals but it would call into question the reliability of future competitive processes for the expansion of natural gas service in Ontario and furthermore deny EPCOR the opportunity to earn a reasonable return. EPCOR's position on these issues is summarized as follows:

    a. **In accordance with the ten-year regulatory compact, EPCOR's Rates 1 and 6 South Bruce customers bear the risk of average customer volumes throughout the ten-year rate stability period.** EPCOR's South Bruce operation is based on a well thought out and balanced ten-year regulatory compact, wherein some risks were meant to be borne by the utility and others by the ratepayers. This ten-year deal was the outcome of a highly regulated, competitive process that involved the development of common infrastructure plan applications (CIP) by proponents seeking to expand natural gas service in South Bruce. The CIP submissions detailed the proponents' revenue requirement to serve specific South Bruce communities and consisted of common assumptions for which the utilities did not assume risk as well as competitive parameters for which the utilities assumed full risk. The regulatory history is clear that average volumes for Rate 1 and 6 customers was a common assumption in the CIP for which the risk was borne by ratepayers. The bright line between what elements the utility bears risk for and what it does not, persists throughout the ten-year rate stability period and should not be disturbed or dismantled on a piecemeal basis.

    b. **Based on prior regulatory approvals, EPCOR is entitled to full recovery of amounts recordable in the CVVA.** The OEB previously determined that rates approved in EPCOR South Bruce's 2019-2028 Custom IR proceeding must be consistent with the CIP.[3] Accordingly, the proposed CVVA will help to restore and fully implement the underlying utility-customer risk sharing framework set out in the CIP

[3] Southern Bruce Expansion Applications, Decision and Order, April 12, 2018, Section 4.2 Assessment of CIP Proposals, p. 11.

and which was approved at the outset by the OEB during the competitive process. This outcome will enable EPCOR to collect rates consistent with the utility's approved revenue requirement, which will remain unchanged. EPCOR relied on this risk sharing framework in its entirety as it continued to buildout the distribution system and connect customers as committed to in the regulatory compact. In the context of a 10 year regulatory compact, it is only fitting that a discrepancy between a forecasted common assumption and its actual value needs to be addressed.

c. **The proposed CVVA is required for EPCOR to earn a reasonable return on its investment.** The utility is already in a position of under-earning[4] due to variances in actual versus forecasted customer volumes for Rates 1 and 6 customers and cannot absorb such revenue losses through implementation of efficiencies or cost cutting activities. EPCOR has filed evidence in this proceeding which shows there has been and will continue to be material financial impacts to the utility if the CVVA, as filed, is not approved.[5] As a result of this issue, from 2019 to 2023 the utility has already experienced an estimated revenue shortfall of $1.02 million which is equal to approximately 8.8% of distribution revenue earned during that period.[6] Furthermore, the utility has forecasted an average reduction of the ROE from the years 2019 to 2028 of 3.97%, with the greatest forecasted reduction of the ROE in 2028 of 6.12%.[7] The absence of a CVVA would result in EPCOR recording a total revenue shortfall of $7.81 million by 2028, equivalent to a 13.3% reduction of the approved revenue requirement.[8] This shortfall would reduce the total expected net income from $6.1 million to a loss of $1.8 million over the ten-year term, resulting in a negative cumulative return on equity.[9] During this period the utility is forecasting to keep its expenses consistent with the approved CIP. These outcomes simply do not allow the utility to earn a fair return on its investment. Furthermore, the inability to fully recover

[4] In the year 2020, EPCOR incurred a loss of $2,144,240, as described on p. 35 of the ENGLP Southern Bruce – 2023 IRM Application.
[5] See the ENGLP Southern Bruce 2023 IRM Application dated July 18, 2022, p. 35; ENGLP Response to OEB Staff 3(k)(ii), (i), and (l), filed September 19, 2022; ENGLP Additional Evidence, Phase 2- CVVA, filed November 14, 2022.
[6] ENGLP response to OEB Staff 3(i), filed September 19, 2022.
[7] ENGLP Additional Evidence, Phase 2 – CVVA, filed November 14, 2022, p. 1.
[8] ENGLP Southern Bruce -2023 IRM Application at p. 32.
[9] *Ibid.*

all amounts recordable in the proposed CVVA would impact EPCOR's ability to continue to build out its system and expand natural gas service to other communities in South Bruce such as Brockton.[10]

11. EPCOR recognizes that the proposed CVVA will result in bill impacts to customers served by the South Bruce distribution system. However, the resulting costs to customers are based on the approved 10-year revenue requirement and is not only consistent with but is the risk sharing framework approved by the OEB.

12. Finally, throughout this proceeding, EPCOR has updated and fine-tuned its evidence, including providing illustrative examples and step-by-step explanation on the allocation and disposition methodology for the proposed CCVA. EPCOR is confident that the methodologies as amended (through Additional Evidence filed on November 14, 2022, and in responses to written interrogatories on the Additional Evidence filed on December 5, 2022) are sound and consistent with the stated intent of the proposed variance account. We note that a technical conference was tentatively scheduled for the parties to address any outstanding questions or concerns regarding this issue. However, on December 7, 2022, OEB Staff and intervenors filed a shared letter indicating that a full technical conference was not warranted and instead requested that EPCOR answer brief follow-up questions that were set out in the letter. Accordingly, the OEB by way of Procedural Order No. 4, dated December 8, 2022, cancelled the technical conference and directed EPCOR to answer the additional questions.

C. BACKGROUND/ARGUMENT

a) Multi-phase process resulting in EPCOR receiving approval of Franchise Agreements and CPCNs to serve South Bruce

13. The genesis of EPCOR's South Bruce operations was a generic proceeding commenced by the OEB to review opportunities for natural gas expansion in Ontario and determine how those opportunities should be awarded in the event that multiple utilities were interested in providing

[10] See response to OEB Staff 3(k)(i), filed September 19, 2022 and OEB Staff 4, filed October 20, 2022. Per response to SEC 7 (b), filed October 20, 2022 at p. 24, EPCOR is planning on using the South Bruce rate structure in order to achieve operational and regulatory synergies in the expansion.

the service.[11] This generic proceeding was triggered by EPCOR Southern Bruce Gas Inc. (EPCOR's predecessor) filing applications seeking approval for franchise agreements and CPCNs to serve South Bruce municipalities (the South Bruce Expansion Applications).[12] The South Bruce Expansion Applications were placed on hold pending the outcome of the generic proceeding.

14. In the course of processing the South Bruce Expansion Applications and consistent with the outcome of the generic proceeding, the OEB held a competitive process to determine which utility would receive CPCNs for the Southern Bruce municipalities, as both EPCOR and Union Gas confirmed their interest in servicing these areas. This competitive process required proponents to submit CIPs for the OEB to be able to appropriately assess and compare the value propositions of EPCOR and Union Gas who both wanted to serve the same area. The CIP would serve as the basis for proponents to determine their respective revenue requirements over a ten year rate stability period.[13]

15. The OEB undertook a process to determine the common parameters for the CIP, which were confirmed after a joint session with Board staff and the project proponents and an oral hearing.[14] In summary, there were two categories for CIP parameters being (i) "common assumptions" and (ii) "competitive parameters". Generally, forecasted volumes for common assumptions represented industry averages and therefore the successful proponent did not accept any risk for achieving them. This principle was confirmed in the South Bruce 2018-2028 Custom IR Rate Application (South Bruce Rate Application) when the OEB approved the Energy Content Variance Account.[15] In contrast, the successful proponent would take on the risk on achieving forecasted competitive parameters.

16. In the CIP, there were three common assumptions for which forecasts were used and this included customer consumption for mass market customers (inclusive only of Rates 1 and 6

[11] See EB-2016-0004 (Generic Proceeding).
[12] See EB-2016-0137/EB-2016-0138/EB-2016-0139 (South Bruce Expansion Applications).
[13] Partial Decision on the Issues List and Procedural Order No. 6, June 27 2017, p. 4.
[14] South Bruce Expansion Applications, Procedural Order No. 8, August 22, 2017.
[15] South Bruce Rate Application, Decision and Order dated November 28, 2019, pages 20-22, EB-2018-0264.

for EPCOR). The OEB confirmed customer consumption as being a non-competitive element when it selected EPCOR as the successful proponent, and stated the following:

> *Customer Consumption: Proponents were to use common consumption levels for each mass market segment, except for large commercial or industrial customers, which were to be left to competition.*[16]

17. EPCOR was the successful proponent of the competitive process and received the necessary CPCNs to serve the South Bruce municipalities on April 12, 2018. In that decision, EPCOR was directed as follows, "…*the OEB will require EPCOR to demonstrate that the forthcoming leave to construct and rates applications are consistent with its CIP proposal*."[17] This exact direction was reiterated by the OEB in the South Bruce Rate Application[18] and emphasized in the determination of the issues list, as follows:

> *The OEB understands that there are unique aspects to this rate application given the CIP. A number of cost parameters and rate components have been determined through a prior OEB approved process (competition for the franchise of South Bruce).3 P.O. No. 3 stated that the OEB "will not be revisiting the overall commitments (with the exception of any proposed adjustments) that were made in the CIP process…*[19]

18. The OEB determined at the outset that the regulatory framework established for this community expansion, including the associated utility-customer risk sharing framework as set out in the CIP, would need to be reflected in rates.

b) Forecasted Volumes and the South Bruce Rate Application

19. The common assumptions regarding annual customer volume for mass market customers were based on Union Gas' then current normalized average consumption per customer for its adjacent markets. As there was no existing gas utility servicing the South Bruce area, it was reasonable to accept the normalized average that Union was using in its adjacent territory.

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[16] South Bruce Expansion Applications, Decision and Order, April 12, 2018, p. 8
[17] *Supra note 17,* section 4.2 Assessment of CIP Proposals, p. 11.
[18] South Bruce Rate Application, Decision and Order dated November 28, 2019, p.5, EB-2018-0264.
[19] South Bruce Rate Application, Decision on Issues List dated August 20, 2019, p.3, EB-2018-0264.

20. When EPCOR filed its South Bruce Rate Application it had no reason to believe that the actual average volume per customer would be materially different than the forecasted value agreed upon as between EPCOR, Union and the Board during the competitive process. There was no indication that achieving these forecasted values represented a material risk to the ratepayer or utility and therefore disadvantage either.

21. As a greenfield utility, EPCOR did not have access to historical customer usage data for the South Bruce region to use in setting rates. The discrepancy between forecasted and actual customer volumes and its materiality has only recently come to light now that the South Bruce system has been operating for a period of time and certainly could not have been known with certainty until well after the first South Bruce mass market customer was connected in Q3 of 2020.

22. At the time of the rate proceeding, EPCOR did not anticipate, nor could it have completed any meaningful analysis to confirm the existence of a material usage shortfall. Now that this discrepancy has come to light and can be confirmed through meaningful analysis, it needs to be addressed in order ensure alignment with the approved ten-year regulatory compact. The requested CVVA is the appropriate mechanism to accurately reflect the risk apportionment previously approved by the Board for South Bruce.

23. Notably, Union Gas had an existing variance account to record the differences between forecast and actual values and would therefore not have been taking the risk of achieving forecasted consumption values if they had been the successful proponent.

c) Under-Generation of Revenue Associated with Forecasted Volumes

24. EPCOR has recorded consumption volumes since connecting its first South Bruce customer and has determined that for residential customers, their actual consumption is less than the forecasted value included as a common assumption in the CIP. Although as a greenfield utility EPCOR does not have long term consumption data for its customers it has forecasted

a shortfall of approximately 696 m^3 or 32% per year in reference to the common assumption of 2,149 m^3.[20]

25. As described earlier in the submission, this variance has already resulted in a material under-generation of revenue for EPCOR and based on current trends, the utility's financial position will be further materially impacted.

26. If the CVVA is not approved or if EPCOR is not permitted to recover all recordable amounts, it will immediately place EPCOR in a material revenue deficiency and result in the utility chronically starting from a position of under-earning over the course of the rate stability period and not being able to expand its distribution system. Setting rates on this basis will prevent EPCOR from earning revenue in accordance with its approved revenue requirement and will not allow the utility to earn a fair return on its investment. This outcome would be contrary to standard ratemaking principles and the statutory objects of the OEB Act.

d) Establishing the CVVA

27. Approval of the proposed CVVA is essential to recognize the principle of risk sharing that was agreed to by all parties (including the OEB) and that EPCOR has been relying on as it continued to build out the distribution system and connect customers in the South Bruce area.

28. Although in the original application, EPCOR requested an effective date of January 1, 2020 for the CVVA, EPCOR has amended the effective date to January 1, 2021.[21] This revised date aligns with the timeframe within which EPCOR relied on the revenue generated from a common assumption related to the forecasted volume consumed by mass market customers and prior to this revised effective date there is insufficient data for EPCOR to appropriately calculate amounts recordable in the proposed variance account.

29. EPCOR is seeking an end date for recording amounts in the CVVA of December 31, 2028 as that is the end date of its current ten-year Custom Incentive Rate plan.

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[20] ENGLP Southern Bruce – 2023 IRM Application, filed July 18, 2022 at page 31.
[21] Supplementary IR Responses, OEB Staff 4 (a), filed December 5, 2022 at p. 8.

D. RELIEF REQUESTED

30. For the reasons set out in this submission, EPCOR respectfully requests that the OEB approve the proposed CVVA, including the proposed allocation and disposition methodologies, as filed and amended, in this proceeding.

All of which is respectfully submitted.