Shepherd Rubenstein

BY EMAIL and RESS

Mark Rubenstein
mark@shepherdrubenstein.com
Dir. 647-483-0113

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

January 27, 2022
Our File: EB20220184

Attn: Nancy Marconi, Registrar

Dear Ms. Marconi:

Re: EB-2022-0184 – EPCOR Natural Gas LP Phase 2 – SEC Submissions

We are counsel to the School Energy Coalition ("SEC"). Pursuant to Procedural Order No. 3, these are SEC's submissions on the request by EPCOR Natural Gas Limited Partnership ("EPCOR") for approval of its proposed Customer Volume Variance Account ("CVVA"), as well as the allocation and disposition methodologies.

SEC submits the OEB should deny the request for the proposed CVVA. EPCOR's Custom IR application set the rate framework for the rate stability period (2019-2028) and it did not include any adjustments for variances in customers' normalized average consumption. The bargain struck with connecting customers until 2028 should not be disturbed.

If the OEB does determine that the approval of the CVVA is appropriate, then the burden should be shared between customers and EPCOR, the account should not be retroactive, and its application should be limited in geographic scope. Additionally, the OEB should require information to be distributed to both existing and potential customers regarding the impacts of the CVVA and the forecast bill impacts.

Background

EPCOR was selected to serve the communities of Southern Bruce[1] by way of the OEB's competitive Common Infrastructure Plan ("CIP") process[2], that arose as a result of the Generic Proceeding on Community Expansion.[3] As part of that CIP process, proponents who sought to construct a new greenfield utility to serve the Southern Bruce communities filed proposals based on a common set of

[1] Specifically, the Municipality of Kincardine, Township of Huron-Kinloss., and the Municipality of Arran-Elderslie, excluding the geographic area of the former Township of Arran and the former Village of Tara.

[2] *Decision and Order* (EB-2016-0137/138/139), April 12 2018

[3] *Decision with Reasons* (EB-2016-0004), November 17 2016

agreed upon parameters. One of those agreed upon parameters was average consumption volume for each customer type. The successful proponents' CIP proposal was to be the basis for the derivation of the revenue requirements and rates over a 10-year rate stability period.[4]

After being selected as the successful proponent, as required, EPCOR filed a Custom IR rate application to cover the mandated rate stability period (2019-2028)[5]. As part of the application, EPCOR forecast annual revenue based on a forecast number of customers, their types, and their average annual consumption, which were included as part of the CIP process.[6] The outcome of that proceeding, which included a partial settlement, was approval of rates effective January 1, 2019[7], and a rate framework for the remainder of the 10-year rate stability period.[8] The approvals included, among other things, a mechanism for annual adjustments and a number of deferral and variance accounts ("DVAs").[9]

Whereas the CIP process can be said to have determined the 'rules' regarding the scope of the rate application that EPCOR would have to file with the OEB, the Custom IR application can be said to have determined the 'rules' regarding what customers would have to pay for gas distribution service during the rate stability period.

As EPCOR started building and connecting customers to its new natural gas system in the Southern Bruce communities, it discovered that the average customer consumption parameter that it had agreed to use in the CIP process, and was subsequently used in setting rates, did not reflect the actual average customer consumption of these new customers. Weather normalized average customer volumes are approximately 32% less than was assumed during the CIP.[10] The variance is most acute with respect to Rate 1 customers, where primarily residential customers' consumption is materially lower than the CIP common parameter, leading to a significant and growing revenue variance compared to what was approved for each year.[11]

For Rate 6 customers, the rate class that schools are (or will be) in, the difference is more muted. In 2021 and forecast for 2022, average customer consumption was higher than was forecast as part of the CIP process, but beginning in 2023 EPCOR forecasts the average customer consumption will be slightly lower each year.[12]

CVVA Balance									
	2021A	2022F	2023F	2024F	2025F	2026F	2027F	2028F	Total
Rate 1	$134,883	$494,412	$809,009	$1,130,134	$1,276,998	$1,304,911	$1,335,662	$1,366,205	$7,852,214
Rate 6	-$13,895	-$75,384	$5,887	$4,166	$18,603	$18,873	$19,444	$16,991	-$5,314
Total	*$120,988*	*$419,028*	*$814,896*	*$1,134,301*	*$1,295,601*	*$1,323,783*	*$1,355,106*	*$1,383,197*	*$7,846,900*
Source: EPCOR_IRR_CVVA_excel_20221205 (Summary Tab)									

[4] *Decision and Order* (EB-2018-0264), November 28, 2019, p.8
[5] EB-2018-0264
[6] EB-2018-0264, Application, Exhibit 3
[7] *Rate Order* (EB-2018-0264), January 9, 2020
[8] *Decision and Order* (EB-2018-0264), November 28, 2019; *Decision on Settlement Proposal and Procedural Order No.6* (EB-2018-0264), October 3, 2019, Schedule A, Settlement Proposal, September 16, 2019, p.19
[9] *Rate Order* (EB-2018-0264), January 9, 2020
[10] Application, p.31
[11] Application, p.31; IRR Staff-1 (October 20, 2022); Updated in Additional Evidence (November 14, 2022), p.2
[12] IRR Staff-1 (October 20, 2022)

The reason for the variance between actual average customer consumption and the agreed upon CIP parameter, which was based on Union Gas's historic average, are entirely reasonable and were foreseeable. At the time customers switch to natural gas, they do not replace each and every one of their existing appliances that can be converted to natural gas.[13] They replace them over time as those appliances reach their end of life.

As part of this application, EPCOR seeks approval of a CVVA, to capture the difference in actual weather normalized average customer volumes from what was approved as part of its rate application for the rate stability period, with retroactive effect back to January 1, 2021. It also seeks approval for its proposed disposition methodology of the balances.[14] EPCOR proposes to capture the variance, and to collect or refund the balance to/from customers, calculated on a rate class specific basis.

EPCOR argues that the establishment of its proposed CVVA is appropriate since the average customer consumption volumes were a common assumption as part of the CIP process, and were not one of the components in its proposal in which the successful proponent was supposed to bear any risk.[15] It claims that without the CVVA as proposed, it would be in an under-earning position during the rate stability period, not allowing it to earn a fair return on its investment, and that they would not be able to expand the distribution system.[16]

The result is that under EPCOR's proposal, Rate 1 customers can expect a very significant increase in their bills, and Rate 6 customers a very small decrease, over the rate stability period.[17]

SEC notes that bill impacts shown in interrogatory response SEC-6 have not been updated to reflect the corrected balances EPCOR has filed.[18] Thus, the bill decrease for Rate 6 customers shown in that response for beginning in 2025, if updated, would show a bill increase. Regardless of the forecast, since most forecast customers during the rate stability have yet to connect[19], it is hard to accurately forecast what any future average volumes (and so CVVA balance) will be, especially with respect to medium to large customers.

Should the OEB Approve the CVVA?

SEC submits the OEB should not approve the proposed CVVA.

While SEC does not dispute that as part of the CIP process, the average volume per customer was a common assumption, what that meant is that EPCOR had the right as part of its Custom IR application to bring forward a proposal to deal with that specific risk. What it cannot do, after having had its rate framework approved, on which both connecting and soon to be connecting customers have relied, is to change the bargain struck during a period which is explicitly about rate stability.

[13] Application, p.31

[14] Argument-in-Chief, para.1, 8

[15] Argument-in-Chief, para.110,

[16] Argument-in-Chief, para 25-26

[17] IRR SEC-6 (October 20, 2022)

[18] In the IRRs on the Additional Evidence, EPCOR made corrections to the account balances (See cover letter to EPCOR IRR (December 5, 2022, corrected information contained in the 'Summary' tab of file EPCOR_IRR_CVVA_excel_20221205).

[19] IRR OEB Staff-2 (December 5, 2022)

Connecting customers to EPCOR's system are in a different situation than most other natural gas customers in the province. Those new customers have had to make significant and costly upfront investments on their side of the meter to begin to receive natural gas. Those decisions are generally based on understanding the payback period that would result from savings by switching some of their energy supply needs to natural gas. For many customers, including medium and large customers, they have to make the decision to switch to gas long before actually connecting and receiving service. They need to order (and pay) for customer-side equipment and make installation arrangements. From a customer's perspective, the information they had as the input to that analysis, which includes understanding delivery rates during the rate stability period, are based on the approvals sought and received from the OEB as part of the Custom IR application. As part of those approvals, EPCOR never sought a variance account or other form of an adjustment mechanism to deal with variances in average customer consumption.

EPCOR's evidence is not that it forgot to request the CVVA as part of its Custom IR application, nor that it mistakenly believed a specific DVA approval was not needed. It was simply the case that it did not think that there would be a material variance in average consumption necessitating a DVA.[20] In response to interrogatory Staff-3, EPCOR stated that it "would have applied for the CVVA in the 2019-2028 proceeding, however, the common customer consumption assumption, as approved by all parties, was based on historical consumption in adjacent regions, and there was no indication that achieving it represented a material risk to the ratepayer or utility and therefore no disadvantage to either."[21]

EPCOR later turned its mind to the issue, and determined that there was an immaterial risk. It should not be allowed, years later, to change its mind when the risk materialized to its detriment. SEC finds it highly unlikely that if the opposite had occurred (average annual consumption was materiality higher than the CIP common assumption), EPCOR would have requested the CVVA.

While the EPCOR Southern Bruce system is greenfield, EPCOR and its parents are not new to the natural gas business.[22] The company is a highly sophisticated and experienced gas distributor, and even had some Ontario experience with its purchase previously of the Aylmer territory from NRG.[23] It was also not shy to seek approval in the Custom IR for many different DVAs to transfer cost and revenue risk including, among others, those for heat content, municipal taxes, and regulatory costs.[24]

Furthermore, even though during the CIP process, average customer volumes was a common parameter, that value was not set by the OEB. It was agreed upon by the proponents, which included EPCOR, and submitted to the OEB.[25]

EPCOR's request is also unfair as it undermines the integrity of the partial settlement achieved in its Custom IR application. If EPCOR had requested such an account in that proceeding, the bargain reached between intervenors and the company would likely have been different.

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[20] IRR Staff-3 (September 19, 2022)

[21] IRR Staff-3 (September 19, 2022)

[22] EB-2016-0137/138/139, Southern Bruce Common Infrastructure Plan Application, October 16, 2017, p.8-13

[23] *Decision and Order (*EB-2016-0351), August 3, 2017

[24] *Rate Order* (EB-2018-0264), January 9, 2020, p.5

[25] *Decision on Preliminary Issues and Procedural Order No. 8* (EB-2016-0137/138/139), August 22, 2017, p.5

EPCOR's arguments about the financial impacts of the under-recovery without the CVVA needs to be considered in the proper context.

First, the statutory requirements of the *Ontario Energy Board Act*, in setting just and reasonable rates, only requires that over the *long-run* EPCOR is given an *opportunity* to earn a fair return on its investment (i.e. its approved ROE).[26] Although it may under-earn, even materially, during the rate stability period, that is due to its own actions, and EPCOR should not now be bailed out by ratepayers. Even in a decarbonizing environment, these assets and newly connected customers will likely remain on gas for the foreseeable future, allowing the company to earn a fair return over the long-term.

Second, while EPCOR mentions in passing in its argument that it will not be able to expand its distribution system, it has filed no evidence in this regard. This is despite being given the opportunity to file additional evidence related to the financial impacts should the OEB not approve the CVVA as proposed.[27] No evidence was filed at all regarding impacts on expansion plans, nor any information regarding the practical implications of denial of approval, for example on debt credit metrics, that one would have expected if the impact was so severe as to potentially impact EPCOR's financial viability. The reason for this is that it will not actually harm its financial viability. It admits as much as it relates to its parent.[28]

Third, SEC notes that as part of the approved partial settlement proposal in the Custom IR application, the parties agreed that EPCOR would not be eligible for the generic +/- 300 basis earnings off-ramp.[29] This is an indication, as part of the package settlement, that EPCOR's financial viability would not be at risk if its ROE was below that level, and so did not require the ability to seek extraordinary relief from the OEB in such a circumstance.

For all of the above reasons, SEC submits that the proposed CVVA should not be approved as it s inappropriate, and unfair to both existing and potential new customers.

If the OEB Does Approve the CVVA, What Are The Appropriate Terms and Conditions?

In the alternative, if the OEB determines that the CVVA, in some form, should be established, it should only do so based on terms and conditions that are fair.

Sharing of the Burden

EPCOR's shareholders should share in the burden of the under-recovery. It is entirely unfair that during the rate stability period ratepayers should bear the entire consequences of EPCOR's misjudging average customer consumption during both the CIP process and the Custom IR application.

SEC submits a potential approach would be similar to the OEB's policy regarding recovery of the impacts arising from COVID-19.[30] The OEB determined the burden should be shared, and for non-

[26] *Ontario Energy Board v. Ontario Power Generation Inc.*, 2015 SCC 44, paras 16-17

[27] See Additional Evidence filed on November 14, 2022

[28] IRR Staff-3(i),(m) (September 19, 2022)

[29] *Decision on Settlement Proposal and Procedural Order No.6* (EB-2018-0264), October 3, 2019, Schedule A, Settlement Proposal, September 16, 2019, p.19

[30] *Report of the Ontario Energy Board: Regulatory Treatment of Impacts Arising from the COVID-19 Emergency* (EB-2020-0133), June 17, 2021 p.17

exceptional pool costs (i.e. those not incurred to meet government or OEB-initiated programs), the OEB would require 50/50 split between customers and the utility, for costs below the deadband amounts (300 basis points). There would be no recovery of the amounts related to the difference in average use that fall within the deadband, only the amounts that contribute to earnings variance below (or above) 300 basis points.[31]

In this case, the 300 basis points deadband would be calculated as a comparison between earnings with and without the CVVA. This ensures that EPCOR recovery is only based on the average customer consumption variance, and no other aspects. The mechanism should also be symmetrical, and any sharing should be on a rate class specific basis.

Notice to Potential and Existing Customers

If the CVVA is approved, regardless of the specifics, it is critical that the existing and potential new customers are made aware of the implication on their costs during the remainder of the rate stability period. Potential customers in the Southern Bruce communities are making decisions today regarding connecting to the natural gas system. The material they may have been given, and the rate information in the approved rate order and Custom IR framework will not reflect the true amount they will have to pay. Customers who have already connected should also be made aware. Since the impact is through a DVA disposition as opposed to being included in base rates, those customers cannot accurately take the impact into account when making real time consumption decisions, so providing this information now is important.

The OEB should explicitly require EPCOR to:

a) Notify any existing customers and any potential customers that have expressed any interest in service but have not actually started receiving service yet, with the information, and revised bill forecasts, including express notice that past impact information is no longer valid or reliable; and
b) Update all marketing material and other information which may be provided to potential new customers, regardless of the communication method, to explicitly include the impacts of forecast CVVA disposition, consistent with the information filed in this proceeding, in any presented bill impacts, energy cost savings, and payback period estimates. The material and information should also tell those that the amounts may change based on average consumption of customers across the communities.

Effective Date

EPCOR proposes an effective date for the CVVA as January 1, 2021. SEC submits that the earliest the OEB can make the account effective is at the release of its final decision in the proceeding. To do otherwise, would be impermissible retroactive ratemaking.

The OEB is prohibited from recovering amounts from utilities or customers related to a previous period unless it falls under one of the known exceptions to the rule against retroactive ratemaking.[32] The two general exceptions to the rule against retroactive ratemaking are rates declared interim, or the

[31] *Report of the Ontario Energy Board: Regulatory Treatment of Impacts Arising from the COVID-19 Emergency* (EB-2020-0133), June 17, 2021 p.15
[32] *Union Gas Limited v. Ontario Energy Board*, 2015 ONCA 453, para. 88-89

existence of a deferral (or variance) account.[33] Neither are applicable here, since rates have not been interim and there is no approved CVVA (or any other account) tracking the variances.

An analogous situation is that of Halton Hills Hydro's 2018 IRM application.[34] In that matter, Halton Hills Hydro applied to the OEB to establish a new DVA account to record an adjustment to its revenue requirement related to an error it made in its 2016 rebasing application regarding its depreciation expense, effective beginning in 2016.[35] In its decision, the OEB denied approval of the retroactive effective date.[36] As the OEB noted, although it "has broad powers to set just and reasonable rates….. the rule against rate retroactivity is not discretionary other than for a narrow set of exceptions."[37] It also found, with respect to an Alberta Court of Appeal's comments on knowledge being the critical factor if a retroactive adjustment is permissible, "that [t]he OEB has not previously established an expectation that the rates for 2016 and 2017 could be subject to change."[38] Similarly here, the OEB has not established an expectation to customers that EPCOR's rates have been anything but final.

Geographic Scope

EPCOR proposes that the geographic scope of the CVVA would not just be the Southern Bruce communities, defined as those that were subject to the CIP process, but also new communities that to which EPCOR plans to expand, such as Brockton.[39] SEC submits that if the OEB is going to approve a CVVA, it should be limited to customers that were part of the CIP process. EPCOR bases its argument that it should be granted the CVVA on its claim that, as part of the CIP process, it was never meant to take on weather normalized average customer consumption risk. Given that position, it cannot at the same time argue that the scope should include municipalities that were not part of that same CIP process. That would require a completely different logic.

There may be valid reasons to apply a CVVA to non-CIP process communities, but that should be considered in the context of the appropriate application at the time the request for the relevant leave to construct and rate approvals are sought. It should not occur as part of this proceeding.

Calculation and Disposition Methodology

If the OEB is going to approve the CVVA, subject to terms and conditions discussed above, SEC does not oppose the calculation and disposition methodology as detailed in the Additional Evidence.[40]

SEC expects that a party may argue that the OEB should dispose of any balances across all customer classes, and not undertake separate calculation and disposition for each rate class. This would result in all customer classes (Rate 1, 6 and contract) bearing the total annual CVVA balance forecast (on a per m^3 basis).

SEC submits that such an approach would not be appropriate. EPCOR's proposed approach is the more appropriate method. If the intent of the CVVA is to capture and dispose of the variances in weather normalized average customer use as compared to what was included in the CIP, and then

[33] *Union Gas Limited v. Ontario Energy Board*, 2015 ONCA 453, para. 88-89
[34] *Decision and Order* (EB-2017-0045), April 26, 2018
[35] *Decision and Order* (EB-2017-0045), April 26, 2018, p.17
[36] *Decision and Order* (EB-2017-0045), April 26, 2018, p.19
[37] *Decision and Order* (EB-2017-0045), April 26, 2018, p.19-20
[38] *Decision and Order* (EB-2017-0045), April 26, 2018, p.20
[39] IRR Staff-3k (September 19, 2022); IRR SEC-7 (September 19, 2022)
[40] See Additional Evidence, November 14, 2022, Appendix A

the Custom IR application, then the disposition methodology should attempt to reflect 'what would have happened if the actual weather normalized average consumption' was the basis for rate-setting in the first place.

While the volumetric component of EPCOR's delivery rates was set on the basis of forecast consumption, the allocation of costs amongst the rate classes was not. The allocation of distribution costs amongst rate classes was based on a number of factors, most related to forecast number of customers and demand (i.e. peak, coincident, non-coincident), as opposed to volume. EPCOR has filed no evidence relating to whether the reduction in average customer volumes has similarly impacted demand, and if so by how much. There is not a direct relationship, and often reduction in consumption does not change a customer's annual specific peak demand.

Summary

SEC submits the OEB should deny the request to establish the proposed CVVA.

In the alternative, if the OEB does establish a CVVA, it should modify the terms and scope. The account should be subject to a sharing of the burden between EPCOR and customers, the temporal and geographic scope should be limited, and the OEB should mandate EPCOR provide notice and information to existing and potential customers of the expected bill impact.

Yours very truly,
Shepherd Rubenstein P.C.

Mark
Rubenstein
2023-01-26
17:39:23

Mark Rubenstein

cc: Brian McKay, SEC (by email)
Applicant and intervenors (by email)