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

BY EMAIL

November 14, 2024

Nancy Marconi
Registrar
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto ON M4P 1E4
Registrar@oeb.ca

Dear Ms. Marconi:

Re: Enbridge Gas Inc. (Enbridge Gas)
2024 Rebasing Application – Phase 2
Ontario Energy Board (OEB) Staff Submission on Settlement Proposal
OEB File Number: EB-2024-0111

In accordance with Procedural Orders No. 7 and 8, please find attached OEB staff's submission on Enbridge Gas's settlement proposal for the above noted proceeding. This document has been sent to Enbridge Gas and to all other registered parties to this proceeding.

Yours truly,

KVirani

Khalil Viraney
Case Manager EB-2024-0111

Encl.

cc: All parties to EB-2022-0200/EB-2024-0111

ONTARIO ENERGY BOARD

OEB Staff Submission on Settlement Proposal

Enbridge Gas Inc.

2024 Rebasing Application – Phase 2

EB-2024-0111

November 14, 2024

Introduction

Enbridge Gas Inc. (Enbridge Gas) filed an application with the Ontario Energy Board (OEB) under section 36 of the *Ontario Energy Board Act*, *1998* (OEB Act) seeking approval for changes to the rates that it charges for natural gas distribution, transportation and storage, beginning January 1, 2024. The application included setting 2024 rates on a cost-of-service basis and approval of an incentive rate-setting mechanism (IRM) for the years 2025 to 2028. The OEB is reviewing the application in three phases. This proceeding addresses Phase 2 of the application.

On August 17, 2023, the OEB approved a settlement proposal between Enbridge Gas and the intervenors on some Phase 1 issues.[1] After a hearing on the remaining issues, the OEB issued its Decision and Order on December 21, 2023.[2] An Interim Rate Order for 2024 rates was issued on April 11, 2024.[3]

Enbridge Gas filed its Phase 2 evidence on April 26, 2024. The OEB issued Procedural Order No. 2 on May 30, 2024 setting out the issues list for Phase 2 and procedural steps up to and including the settlement conference.

A settlement conference was held on September 10 to 13, September 18 to 20, and October 7 to 9, 2024, with respect to the Phase 2 issues in the proceeding. Enbridge Gas and 21 intervenors participated in the settlement conference (collectively, the Parties).[4]

Enbridge Gas filed a settlement proposal with the OEB on November 4, 2024. The Parties reached complete agreement on the following Phase 2 issues:

Category	Issue Numbers[5]
IRM	3-6
Storage	9-14
Energy Transition Capital Spending, Technology Fund & Voluntary RNG Program	15 and 16
Operating Expenses	19 and 20
Rate Implementation	21 and 22
Other	23-27
IRM	1,2,7,8 and 18

[1] EB-2022-0200, Decision on Settlement Proposal, August 17, 2023.
[2] EB-2022-0200, Decision and Order, December 21, 2023.
[3] EB-2022-0200, Interim Rate Order, April 11, 2024.
[4] The full list of intervenors that participated in the settlement conference can be found in theJune 28, 2023, pp. 5-6.
[5] The issue numbers correspond with the approved Issues List set out in Procedural Order No. 2 dated May 30, 2024.

The three unsettled issues relate to whether Enbridge Gas's 2024-2028 IRM should include a mechanism to decouple revenue from customer numbers, Enbridge Gas's proposal to change the methodology to calculate the Meter Reading Performance Metric and the proposal to procure low-carbon energy as part of the gas supply commodity portfolio.

OEB Staff Submission on the Settlement Proposal

OEB staff submits that the Parties have provided sufficient explanation in the settlement proposal for why the agreed upon resolution is appropriate, including by citing the applicable sections of the evidence.

OEB staff also notes that, as is typical for a large rate proceeding like this one, a number of stakeholders participated, representing a broad range of perspectives. Many of the most experienced practitioners before the OEB were in the settlement room. OEB staff believes that the settlement represents a positive outcome for ratepayers and adequately protects the public interest.

Draft Rate Order

OEB staff has also reviewed the draft rate order, the working papers and the accounting orders. OEB staff submits that Enbridge Gas has accurately reflected the settlement proposal and the OEB's Phase 1 Decision in the draft rate order including the 2025 IRM adjustment. The bill impacts are in line with the price cap index adjustment agreed to in this settlement proposal, 2025 DSM budget change and further expensing of capitalized indirect overheads. Subject to comments on the inflation factor (discussed later in this submission), OEB staff supports the overall calculation of the price cap index.

In this submission OEB staff will not summarize the settlement proposal but will provide additional context and commentary on some key issues.

One of the main settled items in this settlement proposal is the agreement on an IRM framework for the 2025 to 2028 rate period. On the other issues, the settlement proposal results in a significant reduction to the revenue deficiency as compared to Enbridge Gas's original application. The revenue deficiency (excluding gas costs) in the original application was $17.8 million. As a result of the settlement proposal, the revenue deficiency declined by more than 50% to $8.5 million (reduction of $9.3 million). The revised revenue deficiency is shown in Table 1 of the settlement proposal.

The largest component of the reduction to the revenue deficiency comes from adjustments to cost allocation and capital costs of the Dawn to Corruna project. OEB staff supports the reduction and acknowledges that the adjustment addresses the key concerns regarding the Dawn to Corunna project costs and allocation to the unregulated business.

Below is a discussion on some areas of the settlement:

Incentive Rate-setting Mechanism

The parties agreed on the IRM parameters that will apply for the years from 2025 to 2028. The Price Cap IRM formula[6] is similar to the IRM framework that was approved by the OEB in the MAADs proceeding for the 2019 to 2023 period.[7] Some key elements of the IRM framework are discussed below:

Inflation Factor

Enbridge Gas proposed to use a two-factor inflation factor for rate escalation during the IR term, consistent with the OEB's 4th Generation IRM Report of the Board, where the inflation factor is calculated as a weighted average of inflation in a labour sub-index and a non-labour sub-index.[8] Parties agreed that the inflation factor will be calculated as per Enbridge Gas's evidence and will be the weighted sum of:
a) 75% for the non-labour component (calculated as the calendar year-over-year percentage change in the annual average of Canada's Gross Domestic Product Implicit Price Index Final Domestic Demand (GDP IPI FDD)11 available for the most recent calendar year), and
b) 25% for the labour component (calculated as the calendar year-over-year percentage change in the annual average of Ontario fixed weighted index of Average Hourly Earnings (AHE)12 available for the most recent calendar year).

Enbridge Gas further proposed to use the fixed weighted index of AHE for the labour sub-index as it considered the AHE a more representative measure of price inflation for labour inputs than the average weekly earnings (AWE), and because the AHE is a direct measure of input prices and is more compatible with a Price Cap IR than the AWE.

[6] Price Cap = I – X +/- Y +/- Z + ICM.
[7] EB-2017-0306 and EB-2017-0307.
[8] In the 4th Generation IRM methodology, the OEB-approved inflation factor applied a 30% weight to the labour sub-index measured by the average weekly earnings (AWE) for workers in Ontario and a 70% weight to the non-labour sub-index measured by the Canadian GDP IPI FDD.

OEB staff supports Enbridge Gas's proposed approach as agreed to in the settlement. OEB staff notes that its expert, Pacific Economics Group (PEG), supported Enbridge Gas's proposal to use Ontario fixed weighted index for average hourly earnings as the labour price index in the inflation factor formula. PEG noted that Enbridge Gas's proposed index results in less aggregation bias than the (unweighted) AWE that the OEB has been using in inflation factor formulas. PEG further observed that the accuracy advantage of Enbridge Gas's proposed approach was especially pronounced during recessions and the following year. PEG also did not oppose Enbridge Gas's proposed alternative cost share weights (75%/25%) for the two inflation factor subindexes in the inflation factor formula.[9]

OEB staff has not taken a position on PEG's report given that this matter has not proceeded beyond the settlement stage and OEB staff is not party to the proposed settlement. OEB staff acknowledges that Enbridge Gas's proposed approach to calculate inflation in the price cap formula is slightly different than the OEB's approved inflation factor but for purposes of settlement, OEB staff supports the methodology based on the reasons noted by PEG. OEB staff also reserves the right to argue for a different methodology in future for either Enbridge Gas or other utilities.

For 2025, Enbridge Gas has calculated the inflation factor to be 3.61%. The OEB has used only one decimal place for the inflation factor calculated for electricity distributors and transmitters.[10] In Enbridge Gas's 2020 Rates Application OEB-approved settlement proposal, the parties noted, "All parties agree that in future years Enbridge Gas will use an inflation factor that has only one decimal place, to be consistent with the approach used for electricity distributors regulated by the OEB."[11]

If Enbridge Gas has used an inflation factor of 3.61% to derive 2025 rates, OEB staff does not necessarily object to using two decimal places for deriving 2025 rates for purposes of efficiency given that Enbridge Gas has already filed its draft rate order material supporting the settlement proposal. However, for future rate periods, Enbridge Gas should use an inflation factor with only one decimal place.

X-Factor

In its application, Enbridge Gas proposed an X factor of -1.5% comprised of a productivity factor of -1.5% and a 0% stretch factor. These proposed parameters were

[9] Empirical Research for Enbridge Gas IR, Exhibit M3, Pacific Economics Group LLC, August 13, 2024, p. 9.
[10] OEB letter dated June 20, 2024.
[11] EB-2019-0194, Settlement Proposal, November 28, 2019, p.9.

based on the recommendations of Enbridge Gas's expert, Black and Veatch. OEB staff's expert PEG recommended a productivity factor of -0.20% and a stretch factor of 0.45%. for a total recommended X-factor of 0.25%. OEB staff notes that the OEB has never approved a negative productivity factor for a utility in its ratemaking framework.

In the settlement proposal, parties agreed to an X-factor of 0.28%, comprised of a productivity factor of 0% and a stretch factor of 0.28%. In Enbridge Gas's previous IRM framework (2019 to 2023), the OEB approved a productivity factor of 0% and a stretch factor of 0.3%. A stretch factor of 0.28% is lower than the previous approved stretch factor. OEB staff supports the agreed to productivity factor, stretch factor and the resulting X-factor of 0.28%. The agreed to X-factor is higher than that recommended by PEG and OEB staff submits that the annual price cap index adjustment using the proposed X-factor during the IRM term represents a good outcome for ratepayers.

Z-factor

Parties agreed to set the Z-factor materiality threshold to $6.7 million which is derived by taking the current threshold of $5.5 million and inflate it by the same percentage as the growth in the distribution revenue since 2019. OEB staff does not object to the methodology to calculate the Z-factor materiality threshold and considers the proposed new threshold to be reasonable.

Earnings Sharing Mechanism

The Parties agreed to an asymmetrical earnings sharing mechanism (ESM) where if in any calendar year from 2025 to 2028, the actual utility return on equity (ROE) is greater than 100 basis points above the OEB-allowed ROE, the excess earnings above 100 basis points would be shared 50/50 between ratepayers and Enbridge Gas. Further, earnings more than 300 basis points above the allowed ROE would be credited to ratepayers and the Company, on a 90/10 basis.

OEB staff notes that the agreed to ESM is a better outcome for ratepayers as compared to Enbridge Gas's previous IRM framework for the 2019 to 2023 period. In the Enbridge Gas Distribution and Union Gas Limited amalgamation proceeding, the OEB approved an asymmetrical ESM that shared earnings on a 50/50 basis for all earnings in excess of 150 basis points from the OEB-approved ROE.[12] OEB staff considers the ESM as set out in the settlement proposal to be appropriate.

[12] EB-2017-0306 and EB-2017-0307, Decision and Order, August 30, 2018, p. 29.

Incremental Capital Module

The parties agreed that Enbridge Gas will be permitted to seek ICM treatment for projects that qualify under the OEB's ICM policies subject to certain modifications:

a) The project specific in-service materiality threshold, exclusive of overheads, will be set at $75 million. In Enbridge Gas's amalgamation proceeding, the OEB approved an ICM framework that included a project specific materiality threshold of $10 million.[13] The agreed-to materiality threshold is far greater than $10 million and OEB staff believes that the $75 million threshold would mean that fewer projects would qualify for an ICM and ratepayers would not be faced with further rate increases during the IRM term.
b) Enbridge Gas will not include capitalized overhead costs as part of project costs sought for ICM rate recovery during the IRM term. In Enbridge Gas's first rate application (2019) of its previous IRM framework, the OEB approved the inclusion of indirect overheads in ICM project costs.[14] OEB staff supports the exclusion of capitalized overheads as this reduces project costs and will result in a lower ICM rate rider for any projects approved under the ICM.
c) Enbridge Gas will be permitted (but not required) to seek approval of advanced ICM treatment for a project as part of a leave-to-construct application in accordance with its proposal in its application. This approach provides greater certainty to Enbridge Gas of rate recovery through an ICM rate rider for projects that have received leave to construct approval. OEB staff does not oppose the proposed approach.
d) Parties further agreed that Enbridge Gas's proposal for ICM treatment of Asset Life Extension (ALE) will not be implemented. In response to the Phase 1 Decision, Enbridge Gas proposed a modified approach to treat costs related to extending the life of assets in order to address stranded asset risks. In its application, Enbridge Gas requested approval to group ALE alternatives together for the purpose of requesting ICM treatment. Enbridge Gas requested the ICM criteria to be modified for this purpose and recommended two changes – the first was to exclude the requirement that a project be discrete and have an in-service capital addition of at least $10 million and the second was that the capital addition threshold would not apply to ALE projects. OEB staff supports the agreement to not implement Enbridge Gas's proposed approach. The ICM has been designed to permit utilities to seek funding for large projects that cannot be funded through rates and that are not part of typical annual capital programs. Also, combining a number of projects to seek ICM funding is not aligned with the

[13] *ibid*, pp. 32-33.
[14] EB-2018-0305, Decision and Order, September 12, 2019, p. 29.

objectives of the ICM policy and OEB staff believes that such an approach could create issues such as determining which projects are life extension projects versus normal maintenance. It would also make the task of reviewing the costs and monitoring the implementation of the projects more cumbersome.

IRM Rate Term

Parties agreed that the IRM will apply for the years from 2025 to 2028 inclusive. In its Phase 1 Decision, the OEB determined that Enbridge Gas had not considered the risk of stranded assets emerging from the energy transition in its Asset Management Plan. The OEB directed Enbridge Gas to file, in the next rebasing application, an Asset Management Plan that provides clear linkages between capital spending and energy transition risk. The OEB also directed Enbridge Gas to perform a risk assessment and develop a plan in its next rebasing to reduce the stranded asset risk in the context of system renewal. The question is whether the stranded asset risk needs to be addressed earlier than 2029 which is the rebasing year as per the settlement proposal.

Although OEB staff agrees that the stranded asset risk needs to be addressed soon, the logical and feasible timeline is for 2029 rates. Enbridge Gas is expected to file its Phase 3 application in the first quarter of 2025 for which the decision is expected to be issued in the first or second quarter of 2026. Enbridge Gas will require at least a year to prepare its next rebasing application which includes a number of directives and studies.[15] The next rebasing application is likely to be filed in mid or late 2027. Accordingly, rebasing for 2029 rates is the most logical and feasible option, is consistent with Enbridge Gas's proposal and is aligned with the OEB's typical rate-setting term of five years. OEB staff therefore supports the proposed IRM term ending in 2028.

Alternatives to Gas Infrastructure

Issue number 7 in the Phase 2 Issues List posed the question of how Enbridge Gas should be incentivized to implement economic alternatives to gas infrastructure and the treatment to recover the costs.

Intervenor evidence from Current Energy Group (Exhibit M2) sponsored by Environmental Defence, proposed a number of measures to address the energy transition risk.

The parties agreed in the settlement proposal that Enbridge Gas shall study in its next rebasing application a mechanism to implement differentiated ROEs on different asset types and an Efficiency Carryover Mechanism with a capital efficiency sharing

[15] Phase 1 Decision and Order, December 21, 2023, p. 140.

mechanism.

OEB staff notes that there was limited evidence filed by Current Energy Group on the different options to address energy transition risk.

OEB staff supports considering the above measures at the next rebasing. OEB staff believes that these measures need careful study and analysis to ensure that such measures are appropriate, that there are no unintended consequences and to consider the rate implication of such initiatives. Enbridge Gas needs time to study options, to understand the impact of such options and develop a plan to implement a range of possible options. In addition, the settlement contemplates stakeholder sessions to ensure that there is feedback and dialogue on the options, and the most appropriate outcomes are presented to the OEB at the next rebasing.

There was no settlement on the concept of decoupling revenue from customer numbers. The Parties agreed that the OEB should determine that question through a hearing process.

Storage and Gas Costs

As part of the settlement on storage issues, the Parties agreed that Enbridge Gas will maintain the cap of 199.7 PJ of cost-based storage for in-franchise customers. This cap was determined in the Natural Gas Electricity Interface Review (NGEIR) proceeding.

In the November 2006 NGEIR Decision, the OEB determined that the former Union Gas should be required to reserve 100 PJ of space at cost-based rates for in-franchise customers.[16] The combination of the 99.4 PJ of cost-based storage from the former Enbridge Gas Distribution that existed at the time of the NGEIR decision and the 100 PJ of cost-based storage from Union Gas reserved for ratepayers though the NGEIR Decision results in the current 199.4 PJ of cost-based storage available to Enbridge Gas customers. The NGEIR Motions to Review Decision further confirmed that "the purpose of the 100 PJ cap is to establish a permanent allocation between utility and non-utility storage."[17]

OEB staff supports the agreement to maintain the cap of cost-based storage for in-franchise customers. Considering the risk of the energy transition, OEB staff does not support adding more cost-based storage to rate base as this would further increase the

[16] EB-2005-0551, NGEIR Decision with Reasons, November 7, 2006, p.83.
[17] EB-2006-0322/0340, Decision with Reasons, A Review of Certain Parts of NGEIR Decision of November 7, 2006 and Conducted Pursuant to the Board's Review Decision of May 22, 2007, July 30, 2007, p. 7.

risk of stranded assets. Any future reductions in natural gas consumption will require a corresponding decrease in storage requirements and increasing cost-based storage in such an environment would not be in the best interest of ratepayers.

As part of the settlement, Enbridge Gas has agreed to withdraw its proposal to add 10 PJ of market-based storage. The amount of storage to be included in rates is 217.7 PJ, which is the amount calculated using the aggregate excess methodology for bundled customers and contracted storage space by semi-unbundled customers. The result of this adjustment is that Enbridge Gas will have 18 PJ of market-based storage, and it will manage the reduction from the current 26 PJ to 18 PJ by not renewing contracts as they expire.

Enbridge Gas has further agreed to provide greater transparency on its contracts and decisions regarding load balancing made in advance of the winter. Enbridge Gas will also report on the rationale and justification for its load-balancing decisions. OEB staff supports the proposed approach as it may lead to better load-balancing options for ratepayers.

Parties agreed to Enbridge Gas's proposed harmonized storage cost allocation methodology with one change. The change is that a portion of the cost of all new storage assets providing a storage service starting in 2024 will be allocated annually to unregulated storage operations based on an equal weighting of the relative amount of storage space and deliverability provided by the regulated and unregulated storage operations. The exception is for any new additions adding storage capacity or deliverability, which will always be allocated 100% to unregulated storage. For 2024, this results in an allocation of 62% to regulated storage and 38% to unregulated storage. Table 1 shows how the allocation has been determined.

Table 1: Storage Asset Allocators

Storage Space					**Deliverability**				
Rate Zone	**Year**	**Space Utility (PJ)**	**Space Non Utility (PJ)**	**Space Non Utility%**	**Deliverability Utility (PJ/d)**	**Deliverability Non Utility (PJ/d)**	**Deliverability Non Utility%**	**Non Utility Allocator**	**Utility Allocator**
UGL	2024F	100.0	87.0	46.52%	2.1	1.9	47.50%	**47.0%**	**53.0%**
EGD	2024F	99.4	28.0	21.98%	1.9	0.7	26.92%	**24.5%**	**75.5%**
Combined	2024F	199.4	115.0	36.58%	4.0	2.6	39.39%	**38.0%**	**62.0%**

The utility storage space shown in the table above is based on the space determined in the NGEIR Decision. The Parties agreed that Enbridge Gas will fix its maximum firm withdrawal and dehydration capability for in-franchise customers at 4.0 PJ per day (notionally comprised of 1.9 PJ for the Enbridge Gas Distribution rate zone and 2.1 PJ from the Union rate zones). As can be seen from Table 1, the allocation of storage space and deliverability has been used to determine the utility and non-utility allocator.

Dawn to Corunna Project

With respect to the Dawn to Corunna project, Enbridge Gas requested that the OEB approve a utility rate base addition of $338.8 million for 2024. As part of an overall settlement of the storage issues, the Parties agreed to a $19 million reduction to the amount eligible for 2024 rate base addition, with the updated total amount subject to allocation between regulated and unregulated operations. In relation to the allocation of the costs of the Dawn to Corunna project as between regulated and unregulated operations, 62% of the eligible rate base amount ($198.3 million) will be allocated to regulated storage operations and 38% ($121.5 million) will be allocated to unregulated storage operations.[18]

OEB staff supports the proposed reduction of $19.0 million to the proposed rate base addition of $338.8 million for 2024. OEB staff notes that the initial project estimate for the Dawn to Corunna project in the leave to construct application was $251 million. The decrease is considered appropriate in light of the significant increase to the original estimate and inadequate cost control measures.[19] With respect to the allocation of costs, OEB staff supports the 38% allocation of Dawn to Corunna costs to the unregulated storage operations. In the leave to construct application, Enbridge Gas did accept that the project will be used for utility and non-utility operations but argued that the entire cost of the project should be allocated to the utility business and recovered from ratepayers.[20] In that proceeding, a number of intervenors were concerned with Enbridge Gas's proposal to allocate 100% of the projects costs to the regulated operations.[21] Accordingly, OEB staff supports the proposed approach and is of the opinion that a 38% allocation factor to unregulated operations is appropriate.

[18] The total revised amounts is 338.8 – 19 = $319.8M of which 62% or $198.3M allocated to regulated storage operations.
[19] Exhibit I.1.13-Staff-7, CCC-25, CME-11 and SEC-13.
[20] EB-2022-0086, Undertaking JT2.5 and Exhibit I.1.13-CME-8(d).
[21] EB-2022-0086, Final Arguments of Canadian Manufacturers & Exporters, Federation of Rental-Housing Providers of Ontario, Pollution Probe, School Energy Coalition and the Three Fires Group.

Energy Comparison Information

Enbridge Gas has agreed that beginning 45 days after the filing of the settlement proposal, it will not include statements, including cost comparison charts, related to the relative cost-effectiveness of natural gas heating or to savings that can be achieved with natural gas heating in written marketing materials or reference materials unless it includes a comparison with the relative cost-effectiveness of heating with electric cold climate heat pumps. Enbridge Gas has further agreed that updated materials shall be filed in Phase 3 of the rebasing application, or in a subsequent proceeding, if not complete at that time.

OEB staff supports the revision of marketing materials that includes comparison to newer heating technologies.

In closing, OEB staff commends the Parties for their diligence in developing a settlement proposal that OEB staff believes is in the public interest and will support just and reasonable rates. OEB staff submits that the OEB should approve the settlement proposal as filed.

~All of which is respectfully submitted~