



EB-2011-0210

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

AND IN THE MATTER OF an Application by Union Gas
Limited for an Order or Orders approving or fixing just and
reasonable rates and other charges for the sale, distribution,
transmission and storage of gas effective January 1, 2013.

BEFORE: Marika Hare
Presiding Member

Paul Sommerville
Member

Karen Taylor
Member

DECISION ON PRELIMINARY ISSUE AND PROCEDURAL ORDER NO. 2

March 1, 2012

Introduction

Union Gas Limited (“Union” or the “Applicant”) filed an application on November 10, 2011 with the Ontario Energy Board (the “Board”) under section 36 of the Ontario Energy Board Act, 1998 for an order of the Board approving or fixing rates for the distribution, transmission and storage of natural gas, effective January 1, 2013 (the “Application”). The Board assigned file number EB-2011-0210 to the Application and issued a Notice of Application on December 1, 2011. The application was filed on the basis of US General Accepted Accounting Principles (“USGAAP”).

The Board issued its Procedural Order No. 1 on January 11, 2012, which established the approved list of Intervenors for this proceeding. In addition, Procedural Order No.1 recognized the need for the Board's determination on Union's request for the adoption of USGAAP for regulatory purposes (the "Preliminary Issue") in accordance with the Addendum to Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment (the "Addendum Report").

In Procedural Order No. 1 the Board established a timeline for interrogatories, interrogatory responses, submissions, and reply submissions related to the Preliminary Issue in advance of further procedural steps. In addition, the Board adopted the evidence related to the USGAAP issue from Union's 2012 IRM Proceeding EB-2011-0025 (the "Adopted Evidence").

USGAAP Transition

Background

In its EB-2008-0408 Addendum Report, the Board indicated that a utility adopting USGAAP or an alternate accounting standard other than Modified International Financial Reporting Standards ("MIFRS") had to:

- demonstrate the eligibility of the utility under the relevant securities legislation to report financial information using that standard;
- include a copy of the authorization to use as standard from the appropriate Canadian securities regulatory (if applicable); and
- set out the benefits and potential disadvantages to the utility and its ratepayers of using the alternate accounting standard for rate regulation.

Union provided the decision¹ issued by the British Columbia Security Commission approving the use of USGAAP by Union in multiple jurisdictions (British Columbia and Ontario) for financial reporting purposes. The decision was granted for a period of three years, for Union's financial years that begin on or after January 1, 2012 but before January 1, 2015.

¹ EB-2011-0210, Adopted Evidence, Exhibit B1.5, Attachment 3.

In addressing the benefits of USGAAP, Union stated that the primary benefits are administrative simplicity, transparency and a reduced revenue requirement.

With respect to the reduction in revenue requirement, Union has quantified the decrease in 2013 test year revenue requirement at \$63.6 million. Union also stated that USGAAP will provide more rate stability to ratepayers as it is substantially the same as Canadian Generally Accepted Accounting Principles (“CGAAP”) which is currently used by Union. As noted by Union in EB-2011-0025, the only difference between USGAAP and CGAAP relates to employee future benefits. Union noted that the transition to MIFRS would result in a significantly larger adjustment for employee future benefits costs as well as other additional adjustments.

Union stated that the adoption of USGAAP is consistent with the basis of accounting that Union is already using for external financial reporting. As a result, Union will incur no additional costs if it is permitted to use USGAAP for regulatory purposes. No new adjustments or additional record keeping are required. Union also stated that there is reduced risk of errors associated with multiple ledgers and accounting methodologies.

Union stated that it is not aware of any disadvantages of using USGAAP as opposed to MIFRS. Union notes that Enbridge Gas Distribution Inc. (“Enbridge”) has requested that the Board approve its use of USGAAP for regulatory purposes. It is Union’s submission that should Enbridge’s request be approved, there are not likely to be benchmarking related concerns.

On page 19 of the Addendum Report, the Board addresses the issue of the use of USGAAP as a short-term solution, stating:

The Board cautions utilities that the adoption of USGAAP as a short term solution may be counter-productive. If a utility is required to transition to IFRS for financial reporting purposes a few years after adopting USGAAP, certain transitional issues may not have been avoided, but delayed, and additional costs may be incurred if the utility changes its accounting standard twice. The Board will carefully scrutinize the costs incurred to accomplish two successive transitions if the utility seeks to recover these costs from ratepayers.²

² Addendum to Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment, p.19.

Union stated that its plans with respect to financial and regulatory accounting upon expiry of the exemption will depend upon the status of the convergence of USGAAP to MIFRS. If the accounting standards are converged, no further exemption will be required. If the accounting standards are not converged, Union will examine the facts and circumstances at that time to determine if Union will request to extend the exemption.³ Union noted that any costs associated with changes in accounting standards are not expected to be material. In the circumstance where costs of conversion are material Union would seek recovery through a Z-factor adjustment to rates.⁴

Union stated that it is not seeking recovery of the costs associated with USGAAP transition in this rate application and does not anticipate seeking future recovery of these costs. Union indicated that it has incurred costs less than \$0.100 million in 2011 for the transition to USGAAP and no additional costs are expected to be incurred. The recovery of Union's MIFRS conversion costs has been addressed in the EB-2010-0039 proceeding.

Position of Parties

Submissions were received from the London Property Management Association ("LPMA"), Consumers Council of Canada ("CCC"), School Energy Coalition ("SEC"), Canadian Manufacturers and Exporters ("CME"), Association of Power Producers of Ontario ("APPPrO") and Board staff.

LPMA, CCC, SEC and Board staff supported the request by Union for the adoption of USGAAP for regulatory purposes. CME and APPPrO were also supportive of Union's request but provided some proposed conditions of approval.

Board staff submitted that Union demonstrated the required eligibility under relevant securities legislation, and filed the required copy of the authorization to use USGAAP from the securities regulator.⁵ Board staff concluded that Union's evidence supports the use of USGAAP for regulatory purposes and its proposal is in the best interests of the utility and its ratepayers.

³ EB-2011-0210, Adopted Evidence, Exhibit B1.5 (a) iv.

⁴ EB-2011-0210, Adopted Evidence, Exhibit B1.5 (b) iv.

⁵ EB-2011-0210, Board Staff Submission, p. 4.

Board staff noted that Enbridge has also applied to the Board (EB-2011-0354) to set rates based on USGAAP, therefore Board staff submitted that it has no concerns related to benchmarking.

In addition, Board staff noted that Union's successive accounting standard transition plan depends on the status of the convergence of USGAAP to IFRS. As a result, Board staff stated that the Board cannot assess the full impact of a later transition or convergence by Union at this time. Board staff noted that the Board will have the opportunity to scrutinize the costs of the convergence if (and when) Union seeks recovery of the costs through a Z-factor adjustment to rates.

CCC and SEC adopted the Board staff submission on the Preliminary Issue.

LPMA submitted that it supports Union's request for the adoption of USGAAP because it results in a reduction in revenue requirement, lower costs to maintain one set of accounting records, lower gas distribution rates and a benefit from the alignment of accounting frameworks for financial reporting and ratemaking purposes.⁶

CME also supported Union's request for the adoption of USGAAP for ratemaking purposes. CME stated that the evidence provided by Union demonstrates that a transition from CGAAP to USGAAP, for regulatory purposes, is far less disruptive than a transition from CGAAP to MIFRS. CME requested that Union elaborate on matters related to benchmarking.

CME noted that in proceeding EB-2011-0277 (Exhibit I, Tab 1, Schedule 13, page 5), Enbridge provided the following information which may be of some assistance to the Board:

There appear to be many Canadian regulated utilities which are adopting USGAAP or considering adopted USGAAP. Examples of such companies include MRF, Fortis, BC Alta Gas, TransCanada PipeLines, Union Gas Limited and Hydro One. This would facilitate benchmarking with peer companies which will benefit Enbridge and its stakeholder.⁷

⁶ EB-2011-0210, LPMA Submission, p. 3.

⁷ EB-2011-0277, Ex. I, Tab 1, Schedule 13, p. 5.

CME stated that the evidence in Enbridge's case, as quoted above, may be sufficient to prompt the Board to approve Union's transition to USGAAP request now, under the condition that Union elaborate on matters pertaining to the benchmarking issue in a subsequent proceeding.⁸

APPrO offered conditional support for Union's request. APPrO noted that it will only support Union's request if the adoption results in lower rates for R100, T1, and the newly proposed rate class T2 (as compared to the rates that would result from Union adopting MIFRS).⁹

Union submitted that there is no proper basis for the condition imposed by APPrO. In considering the adoption of USGAAP, the Board should have regard to the benefits to ratepayers as a whole as opposed to the benefits or disadvantages to any particular rate class.¹⁰

Board Findings

The Board approves Union's request to use USGAAP for regulatory purposes.

In doing so the Board is mindful of the specific circumstances governing this application. The inherent efficiencies in allowing Union to use the USGAAP for regulatory purposes given its relationship as a wholly owned subsidiary of an American corporation are compelling.

Union has taken the steps necessary to meet the Board's preconditions for deviation from a transition to MIFRS. Union has procured an authorization from relevant Securities regulators which permit USGAAP to be used for its financial reporting purposes, albeit for a limited term.

Union has also demonstrated that there are some measureable and material advantages to ratepayers associated with the transition to USGAAP as opposed to MIFRS. Union has also acknowledged that the treatment of Post Employment Benefits within the USGAAP regime may create some issues which may require special treatment.

⁸ EB-2011-0210, CME Submission, p. 2.

⁹ EB-2011-0210, APPrO Submission, p. 1.

¹⁰ EB-2011-0210, Union Reply Argument, p. 3.

Union has also addressed the question of the meaning of this transition for benchmarking within the sector. The Board is reasonably satisfied that the use of USGAAP by Union will not compromise the Board's ability to make comparisons with relevant comparators, or to conduct meaningful benchmarking exercises. However, if it becomes apparent that such comparisons and benchmarking exercises are compromised, Union may be obliged to provide information, data and statistics in a form and format which conclusively corrects that deficiency.

The Board's approval of this portion of the Application should not be seen as an erosion in any degree of its preference for MIFRS as the predominant financial reporting system for regulatory purposes. Some deviations have been permitted where, as here, a compelling case has been made, but in general, the Board expects the entities it regulates to adopt, effective January 1, 2012 the MIFRS. This policy is rooted in the Board's interest in effective benchmarking, the consistency of financial results, and the development within the sector as a whole of competence in the use of the financial reporting system which has been adopted by the responsible accounting bodies in Canada. The Board has also issued guidance which recognizes that some modification of the IFRS standard is appropriate within the regulatory environment. The Board notes that the authorization granted to Union by the relevant Securities regulators is time limited, or may be subject to other conditions. Union must develop a plan to address the possibility that the authorization it relies upon will lapse or otherwise become ineffective. If such an event occurs during a period when Union is subject to an Incentive Ratemaking Mechanism, Union will be obliged to develop a plan for presentation to the Board to address any issues arising from the termination of the authorization.

Procedural Matters

A Draft Issues List has been included as Appendix "A" to this Decision. An Issues Conference, involving Board staff, intervenors and the Applicant, will be convened to review the Draft Issues List with the objective of developing a proposed Issues List for presentation to the Board. If necessary, an Issues Day proceeding will be convened following the Issues Conference at which time the Board will hear submissions with respect to any contested issues.

The Board is also making provisions for the filing of written interrogatories. The Board notes that interrogatories must reference the pre-filed evidence and must be filed by issue. The Board also requests that Union file the responses to these interrogatories by issue instead of by intervenor. To facilitate the intervenors' review of the responses to their interrogatories, interrogatory responses for each issue shall be grouped by intervenor within the issue.

The Board has determined that the application will proceed by way of oral hearing.

The Board considers it necessary to make provision for the following matters related to this proceeding. The Board may issue further procedural orders from time to time.

THE BOARD ORDERS THAT:

1. An Issues Conference, involving Board staff, intervenors and the Applicant, will be convened to review the Draft Issues List with the objective of developing a proposed Issues List for presentation to the Board. The Issues Conference will not be transcribed. A Draft Issues List is attached to this Order as Appendix "A". A proposed Issues List will be formulated and presented to the Board at the conclusion of the Issues Conference. The Issues Conference will be held in the Board's hearing room at 2300 Yonge Street, 25th Floor, Toronto, on **March 9, 2012** at 9:30 a.m.
2. If necessary, an Issues Day proceeding will take place on **March 22, 2012** at 9:30 a.m. in the Board's hearing room, at which time the Board will hear submissions with respect to any contested issues.
3. Board staff and intervenors who wish information and material from Union that is in addition to Union's pre-filed evidence with the Board, and that is relevant to the hearing, shall request it by written interrogatories filed with the Board and delivered to Union and all intervenors on or before **April 13, 2012**.
4. Union shall file with the Board complete responses to the interrogatories and deliver them to the intervenors no later than **April 27, 2012**.

All filings to the Board must quote the file number, **EB-2011-0210**, be made through the Board's web portal at <https://www.errr.ontarioenergyboard.ca>, and consist of two paper copies and one electronic copy in searchable / unrestricted PDF format. Filings must clearly state the sender's name, postal address and telephone number, fax number and e-mail address. Parties must use the document naming conventions and document submission standards outlined in the RESS Document Guideline found at <http://www.ontarioenergyboard.ca/OEB/Industry>. If the web portal is not available parties may email their documents to the address below. Those who do not have internet access are required to submit all filings on a CD in PDF format, along with two paper copies. Those who do not have computer access are required to file 7 paper copies.

All communications should be directed to the attention of the Board Secretary at the address below, and be received no later than 4:45 p.m. on the required date.

ADDRESS

Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, 27th Floor
Toronto ON M4P 1E4
Attention: Board Secretary

E-mail: boardsec@ontarioenergyboard.ca
Tel: 1-888-632-6273 (Toll free)
Fax: 416-440-7656

DATED at Toronto March 1, 2012
ONTARIO ENERGY BOARD

Original signed by

Kirsten Walli
Board Secretary

Ontario Energy Board
Decision on Preliminary Issue and Procedural Order No. 2
March 1, 2012

Appendix 'A'

To

Decision on Preliminary Issue and Procedural Order No. 2

Union Gas Limited

EB-2011-0210

Draft Issues List

March 1, 2012

Union Gas Limited
2013 Rates
EB-2011-0210

Draft Issues List

Rate Base (Exhibit B)

1. Does the evidence support Union's forecast level of capital spending in 2013?
2. Does the evidence support the proposed updates to Union's lead/lag study?
3. Does the evidence support Union terminating reporting on new business-related directives from prior facility projects?

Revenues (Exhibit C)

1. Does the evidence support Union's general service demand forecast?
2. Does the evidence support using a 20-year declining trend weather normal methodology?
3. Does the evidence support Union's 2013 Contract Customer Demand forecast?
4. Does the evidence support Union's 2013 S&T forecast?
5. Does the evidence support Union's 2013 Other Revenue forecast?

Costs (Exhibit D)

1. Does the evidence support Union's 2013 O&M budget?
2. Does the evidence support Union's 2013 affiliate charges? Does the evidence support Union's compliance with the Board's "three prong test" (as described by the Board in the E.B.R.O. 493/494 Decision with Reasons)?
3. Does the evidence support the provision for depreciation, amortization and depletion proposed in the 2011 Depreciation Study?
4. Does the evidence support Union's changes to unaccounted for gas?
5. Does the evidence support Union's proposed community investment funding?
6. Does the evidence support Union's proposed Energy Technology Innovation Canada program funding?

7. Is Union's forecast of Employee Future Benefit costs which will be incurred under USGAAP appropriate?

Cost of Capital (Exhibit E)

1. Does the evidence support Union's proposed change in capital structure, increasing Union's deemed common equity component from 36% to 40%. Concurrent with this, Union proposes to use the Board's formula to calculate return on equity.

Revenue Deficiency (Exhibit F)

1. Does the evidence support a rate increase to recover Union's delivery related revenue deficiency?

Cost Allocation (Exhibit G)

1. Does the evidence support Union's Cost Allocation Study methodology changes to the allocation of Oil Springs East costs?
2. Does the evidence support Union's Cost Allocation Study methodology changes to the allocation of Tecumseh metering and regulating costs?
3. Does the evidence support Union's Cost Allocation Study methodology to allocate the cost of system integrity?
4. Does the evidence support Union's Cost Allocation Study methodology changes to allocate the cost of North distribution customer station plant?
5. Does the evidence support Union's Cost Allocation Study methodology changes to classify and allocate the cost of distribution maintenance O&M (meter and regulator repairs)?
6. Does the evidence support Union's Cost Allocation Study methodology changes to allocate the cost of distribution maintenance O&M (equipment on customer premises)?
7. Does the evidence support Union's Cost Allocation Study methodology changes to classify and allocate the cost of purchase production general plant?
8. Does the evidence support Union's Cost Allocation Study methodology to allocate the cost of the Dawn to Dawn-TCPL, Dawn to Dawn-Vector and M12 F24-T services?

Rate Design (Exhibit H)

1. Does the evidence support Union's response to the Board directive to review the M12 and C1 rate-making methodology?
2. Does the evidence support the rates proposed in Exhibit H3, Tab 2?
3. Does the evidence support lowering the breakpoint between small and large volume general service customers to 5,000 m³ per year effective January 1, 2014?
4. Does the evidence support the harmonization of the general service rate structures between the North and South operating areas effective January 1, 2014?
5. Does the evidence support lowering the eligibility for the M4 and M5A rate classes to a daily contracted demand of 2,400 m³ and a minimum annual volume of 350,000 m³ effective January 1, 2014?
6. Does the evidence support introducing an M4 interruptible service offering effective January 1, 2014?
7. Does the evidence support lowering the eligibility for the M7 rate class to a combined firm, interruptible and seasonal daily contract demand of 60,000 m³ effective January 1, 2014?
8. Does the evidence support the split of T1 into two rate classes effective January 1, 2013?
9. Does the evidence support recovering UFG on transportation activity in the winter months for the Dawn to Dawn-Vector transportation service?
10. Does the evidence support approval of modification to the M1 and M2 rate schedules?
11. Does the evidence support approval of modification to the M12, M13, M16 and C1 rate schedules including Schedule A, Schedule A-2013 and Schedule C?
12. Does the evidence support updating the utility/non-utility allocator used to calculate margin for sharing for short-term storage services to 59:41?
13. Does the evidence support approval of changes to the Distributor Consolidated Billing fee to \$0.57 per month per customer?
14. Does the evidence support approval of changes to the Gas Supply Administration Fee?

15. Does the evidence support Union's proposal to eliminate the Late Payment Penalty Litigation (No. 179-113) and the Harmonized Sales Tax (No. 179-124) deferral accounts?
16. Does the evidence support Union's proposal to modify the wording of the Short-term Storage and Other Balancing Services (No. 179-70), Average Use Per Customer (No. 179-118), and the Inventory Revaluation Account (No. 179-109) deferral accounts?
17. Does the evidence support an Energy Technology Innovation Canada deferral account?