unionGas
An Enbridge Company

June 22, 2017

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, 27th Floor
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: Consultation on the Regulatory Treatment of Pensions and Other Post-Employment Benefit Costs
Board File No. EB-2015-0040

The following are the submissions of Union Gas Limited (Union) on the variance tracking account implementation issues identified in the Ontario Energy Board's May 18, 2017 Report on the Regulatory Treatment of Pensions and Other Post-Employment Benefit Costs in the electricity and natural gas sectors.

The Board has determined that it will use the pension and OPEB amounts determined through accrual accounting in rate-setting, unless that method does not result in just and reasonable rates. If the accrual accounting method is used, a variance account will be used to track the difference between the forecasted accrual amount in rates and actual cash payment(s) made, with an asymmetric carrying charge in favour of ratepayers applied to the differential.[1] Carrying charges on the new tracking account will be assessed on the monthly opening account balance at the Board's prescribed Construction Work In Progress (CWIP) rate.[2]

The Board determined that utilities will not be compensated for under-recoveries unless the financial viability of the utility would be compromised by such an arrangement.[3]

The Board proposed that the variance account would be effective from the 1st of the month following issuance of its Report unless otherwise ordered by the Board.[4]

<u>Effective Date of the New Variance Tracking Account</u>

As addressed further below, in Union's view, the variance tracking account should track, on an annual basis, the variance between the pension and OPEB costs included in rates and actual cash contributions. Annual entries would be administratively simpler and would remove the impacts of seasonality related to Union's monthly cash contributions.

[1] OEB Report on Regulatory Treatment of Pensions and OPEBs, May 18, 2017, page 8
[2] OEB Report on Regulatory Treatment of Pensions and OPEBs, May 18, 2017, page 12
[3] OEB Report on Regulatory Treatment of Pensions and OPEBs, May 18, 2017, page 10
[4] OEB Report on Regulatory Treatment of Pensions and OPEBs, May 18, 2017, page 11

The new variance tracking account should be effective on the first day of a utility's next fiscal year. For example, if a utility's fiscal year is the same as the calendar year, the effective date would be January 1, 2018.

An effective date of June 1, 2017 (as implied by the Report) or any other time in 2017 would not give Union sufficient notice to plan and incorporate the impacts of the Board's Report into the following internal/external processes which have already been completed for fiscal 2017:

- Budgeting & Forecasting
- Cash flow modelling
- Financing

An effective date coinciding with the beginning of the next fiscal year would be considered best industry practice as it is consistent with how accounting standards updates are treated by the Financial Accounting Standards Board (FASB). The FASB typically orders accounting standards updates to be effective for the subsequent fiscal year after a certain date.

An effective date coinciding with the beginning of the next fiscal year would also give utilities like Union sufficient time to adjust internal processes as required and to request an accounting order for the new variance tracking account. An accounting order is required to support any journal entries made with respect to the new variance tracking account and to fully comply with Union's external audit process, as is currently required of any new deferral accounts.

Union assumes that the review of any required accounting order applications related to the variance account will be limited to a review of materiality, causation and the likely event that the subject cost will be prudently incurred.

In its June 16, 2017 submission, the School Energy Coalition (SEC) submits that, from a fairness perspective, the effective date for the variance tracking account should be the earliest date for which accrual / cash differentials started to accumulate. While SEC made specific reference to over-recoveries and under-contributions being tracked and ratepayers being compensated for the use of their money, Union submits that any determination in this regard should apply equally to any under-recoveries and over-contributions for which the utility's shareholder should be compensated.

Mechanics of the New Variance Tracking Account

The utility would calculate, on an annual basis, the variance between costs included in rates and the actual amounts contributed to pensions and OPEBs on a cash basis. If the opening balance of the cumulative difference between the costs in rates and cash payments in a year indicated a cash surplus (under-contribution), interest based on the Board's prescribed interest rate for the CWIP would be calculated on the opening cumulative balance, and a journal entry booked for the interest as a payable to ratepayers. Calculating interest on the opening balance in a given year is consistent with all of Union's non-commodity and Quarterly Rate Adjustment Mechanism (QRAM) deferral accounts.

During years where the opening cumulative difference indicated a cash deficiency (over-contribution), no interest entry would be made. An interest entry would only resume when the opening cumulative difference balance returned to a cash sufficiency (under-contribution) position. Any cumulative interest balance at year end would be approved and disposed of in the following year as part of the annual non-commodity deferral account disposition proceeding.

Following is an illustration of how Union expects the new variance tracking account to function:

Calculation of Variance Account Interest Expense

Pension / OPEB Costs in Rates Year 1	Cash Payments Made Year 1	Difference	Interest Expense Year 2*
$48,000,000	$44,000,000	($4,000,000)	$112,400

* Interest expense calculated using CWIP Rate (2.81%)

The Board has indicated that the application of the carrying charges would be asymmetric, similar to the approaches established by the Board for capital cost variances and earnings sharing mechanisms.[5] In Union's view, the application of carrying charges in an asymmetric manner is not consistent with the principle of fairness. While the Board indicates that current ratepayers are in effect lending money to the utility to fund future obligations where pension and OPEB amounts collected in rates are higher than cash payments made by the utility[6], the opposite is true when the utilities contribute more than is being recovered in rates. The application of carrying charges on a symmetrical basis would be fair to all parties.

Manner in Which Carrying Charges are Applied to Balances Tracked in Previously Established Variance Accounts

All of Union's previously established deferral and variance accounts attract carrying charges, at the Board-prescribed rate for approved deferral and variance accounts, on the opening cumulative balance. Certain deferral and variance accounts only begin to attract carrying charges after finalization of the year-end balance.

These carrying charges are applied symmetrically. Any deferral or variance account with a cumulative receivable balance incurs carrying charges in Union's favour, and a cumulative payable balance results in carrying charges in ratepayers' favour.

[5] OEB Report on Regulatory Treatment of Pensions and OPEBs, May 18, 2017, page 10
[6] OEB Report on Regulatory Treatment of Pensions and OPEBs, May 18, 2017, page 10

Requirement to Track Only the Gross Accrual Cost as Opposed to Identifying Amounts Expensed vs. Capitalized

In Union's view, tracking the gross accrual cost would be the preferable approach as opposed to identifying amounts expensed vs. capitalized.

In contrast to tracking only the gross accrual cost, identifying amounts expensed vs. capitalized would be much more complex with little marginal benefit as any differences are expected to be immaterial.

Timing of the OEB's Consideration of a Transition to the Accrual Method for Utilities Currently on Cash

Union has no comments on this issue. Union has historically followed the accrual method.

Timing of Disposition of Both the New and Previously Established Variance Accounts

Union proposes that the disposition of any cumulative carrying charges should occur annually.

Annual disposition is consistent with how non-commodity deferral account balances are currently treated, which is appropriate given the similar nature of non-commodity deferral accounts and any cumulative carrying charges related to the new variance tracking account.

The timely disposition of variance accounts avoids violation of the principle of intergenerational equity and ensures current ratepayers receive the benefit from funds recovered in rates that exceed the utility's cash contributions. Reasonable effort should be taken to refund any amounts payable to the ratepayers at the time that the interest expense was incurred by the utility.

Should you have any questions, please do not hesitate to contact me.

Yours truly,

[Original signed by]

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