Saskatchewan
Rate Review Panel

Report to the Minister Responsible for Crown Investments Corporation of Saskatchewan

Regarding the SaskEnergy Commodity and Delivery Service Rate Application
Effective date April 1, 2019

Report submitted February 4, 2019

SASKATCHEWAN
RATE REVIEW
PANEL

SaskEnergy

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Executive Summary

SaskEnergy submitted an application on September 28, 2018 for an overall 10.8% average bill decrease effective April 1, 2019, which would include the following changes to customers' bills:

- A delivery service rate increase of 3.7% effective April 1, 2019;
- An interim commodity rate decrease effective November 1, 2018 of $3.65/GJ to $2.95/GJ; followed by
- A final commodity rate proposed effective April 1, 2019 that would see a further decrease to $2.65/GJ.

SaskEnergy provided a mid-application update on November 26, 2018, which was further revised on December 3, 2018. This update provided some changes to the revenue requirement resulting in a net forecast revenue shortfall of approximately $.348 million. The heat value was also revised, which resulted in a further decrease in the proposed final commodity rate to $2.63/GJ and approximately $1 million decrease in delivery revenue. SaskEnergy indicated that they were not proposing to change the original delivery rate request as a result of these changes.

The Saskatchewan Rate Review Panel has been appointed as a Ministerial Advisory Committee to conduct a review and provide an opinion of the fairness and reasonableness of the proposed rate changes to the Minister of the Crown Investments Corporation by February 4, 2019.

As part of the review process, the Panel contracted an independent technical consultant to review the application and provide recommendations that would be consistent with the Panel's Terms of Reference. The Panel encouraged public input into the review and held a public meeting to facilitate discussion. The Panel, with the assistance of the consultant, put forward two rounds of information requests and supplementary questions (all posted on the Panel's website), and with its consultant, had individual discussions with SaskEnergy staff to clarify specific answers received.

While reviewing the application, the Panel considered not only the test year implications, but the impact of past applications, forecast and actual results, and the potential of future applications and rate increases. Delivery rates have increased every year since 2013 and rates are expected to continue to increase due to SaskEnergy's ongoing integrity and growth requirements. These delivery rate increases have been mitigated to a certain extent by decreases in the commodity rate and the commodity portion of residential customer bills. Although current natural gas prices have remained low, it is expected over time that natural gas prices will increase and this will drive future commodity rate increases, which would compound the effects of future delivery rate increases.

The Panel's review of the application and the consultant's report highlighted the following matters which focused its deliberations on the fairness and reasonableness of the proposed delivery rates.

- There is a general sense that financial results for the immediate past two to three years have been much better than the forecasts used in the prior rate applications. These higher-than-forecast financial results have not directly benefited ratepayers. Better than forecast results were achieved due to some colder weather conditions, stakeholder-directed restraints on expenses applied subsequent to reviews, other positive expense reductions, and better other revenue realizations compared to original forecasts. These are detailed in the balance of this report and the consultant's report.
- It was noted that actual net income for the year ended March 31, 2018 was $70.2 million, which is more than double the forecast.
- Many of the expense categories are forecast to increase at significantly higher rates than would be expected and higher than inflation.

- The total revenue requirement has increased $17.0 million (6.5%) over the prior year's application forecast and $43.9 million (18.5%) over the prior years (2017-18) actual results.

- O&M expenses are forecast to increase by 8.2% over the prior year's application and by 20.9% over the 2017-18 actual results.

- Other expenses such as depreciation, taxes and interest have also increased by significant amounts.

- Other revenue is forecast to be lower by $4.7 million compared to the prior year's application forecast and $7.979 million (25.0%) lower than actual results for that year (2017-18).

- Weather normalized ROE for the local distribution company over the past five and ten years have, on average, been higher than the target 8.3%.

- The company's total expenditure on technology, including labour, third-party hosting and other external services, as well as current and future capital expenditures, appears to be growing at a higher rate than noted in the past.

These indicators led the Panel and the consultants to undertake a rigorous review of the current application and the reasons for the forecasted increases in expenses and the reduction in revenue from other sources.

The Panel has also requested that SaskEnergy undertake reviews of the following matters prior to the next application to ensure that concerns related to these items are fully addressed.

- It was noted that corporation capital tax has increased over prior years. Part of this is expected as the corporation incurs more debt as a result of increased expenditures on growth and infrastructure. The Panel's consultant noted that the calculations and methodology used to allocate the tax to the local distribution company appeared to result in a higher allocation to the local distribution company than would be expected. As a result of this, the Panel has requested that SaskEnergy review this matter and report to the Panel prior to the next application.

- The Panel's consultant has noted that the calculation of rate base used by SaskEnergy failed to account for interest free capital. This arises due to decommissioning costs that are added to the cost of assets as they are built with an offsetting liability for future costs to be incurred at the time of decommissioning. The Panel has asked that SaskEnergy review their methodology, compare to other utilities, and report to the Panel on their findings.

- SaskEnergy monitors commodity risk by reviewing future potential changes to the Gas Cost Variance Account (GCVA). Currently, the +/- $20 million quantum for the GVCA is a forecasted metric -- this means that rather than wait for the GCVA to reach $20 million before bringing forward an application, the impact that future natural gas prices could have on the GCVA are monitored and if the forecasted GCVA balance is projected to exceed the threshold before April 1 or November 1, an application process is triggered. There is currently no formalized policy that includes a framework for more regular, automatic adjustments to commodity rates to ensure that large balances do not accumulate.

The commodity rate reduction in this application would not fully clear the balance in the GCVA at the end of the test year and would maintain a $3.3 million balance in the account on March 31, 2020. This would appear to contradict the original rationale of the fund to provide SaskEnergy the ability to recover the cost of gas sold to customers without any mark up. Rates are traditionally designed to target a GCVA balance of zero.

In conducting this review, the Panel has identified several risk factors that may impact future rate applications including: natural gas prices, weather, carbon tax, interest rates and collective agreements.

Bill Impacts

Bill impacts from the proposed rate adjustments will vary depending on customer class and usage levels. At average consumption levels, customers in all rate classes are expected to experience overall bill decreases due to reduced commodity rates. These decreases could be impacted by the federal carbon tax, which is expected to be implemented on April 1, 2019. SaskEnergy estimates that residential customers would see a 13% bill increase in 2019 with a $20/tonne carbon tax; commercial small customers will see an 18% increase, and commercial large customers will see a 22% bill increase.

If the proposed rate changes were implemented, SaskEnergy's delivery service rates would remain lower than average for major Canadian centres for all customer classes, and the commodity portion of the bills would be in the mid-point range. Based on this information, the Panel has concluded that SaskEnergy's rates will remain competitive with other jurisdictions if the requested rates are implemented.

Recommendations

Following this review and analysis, the Panel makes the following recommendations to the Minister:

1. **That the proposed delivery service rate increase of 3.7% effective April 1, 2019 be revised to 3.4%.**

2. **That the Panel's approval for the interim commodity rate decrease effective November 1, 2018 of $3.65/GJ to $2.95/GJ be confirmed.**

3. **That the proposed commodity rate effective April 1, 2019 that would see a further decrease to $2.65/GJ be revised to $2.575/GJ to eliminate any outstanding balance in the GVCA by March 31, 2020.**

The reduction of the delivery service rate from 3.7% to 3.4% reflects adjustments for all the changes noted by SaskEnergy in the mid-application update, the adjustment for labour noted by our consultant as well as adjustments to the rate base calculation of interest expense outlined later in this report. These changes result in a ROE of 8.14% as proposed in the mid-application update. Full details of these adjustments are included in the following sections of this report.

The reduction of the final commodity rate is recommended to bring the GCVA to a target nil balance at March 31, 2020. More detail on this adjustment is provided later in this report.

SaskEnergy's Rationale for the Application

SaskEnergy submitted an application on September 28, 2018 for an overall 10.8% average bill decrease effective April 1, 2019, which would include the following changes to customers' bills:

- A delivery service rate increase of 3.7% effective April 1, 2019
- An interim commodity rate decrease effective November 1, 2018 of $3.65/GJ to $2.95/GJ, followed by
- A final commodity rate proposed effective April 1, 2019 that would see a further decrease to $2.65/GJ.

If approved, this increase would result in the following changes to customer's bills:[1]

	Commodity Rate Decrease ($3.65/GJ to $2.65/GJ)		Delivery Service Rate Increase		Total Bill Impact	
	$/Month	Annual Bill % Decrease	$/Month	Annual Bill % Increase	$/Month	Annual Bill % Decrease
Residential	($8.50)	(11.1%)	$1.76	2.3%	($6.74)	(8.8%)
Commercial Small	($39.99)	(14.6%)	$4.47	1.6%	($35.52)	(13.0%)
Commercial Large	($520)	(17.0%)	$16	0.5%	($505)	(16.5%)
Small Industrial	($2,435)	(20.2%)	$13	0.1%	($2,422)	(20.1%)
Average		(12.7%)		1.9%		(10.8%)

Delivery Service Rate

SaskEnergy estimates that it will require an average increase of 3.7% starting on April 1, 2019 to mitigate a revenue shortfall of $10.0 million and to provide an 8.3% return on equity (ROE), and a net income of $33.5 million over the application period.[2]

SaskEnergy indicates that the primary drivers for this increase are ongoing investments related to "safety, system integrity and major growth infrastructure."[3] Other factors leading to the rate increase are regulatory code compliance and industry best practices regarding safety along with SaskEnergy's pipeline integrity and major growth infrastructure programs. The specific drivers underlying the overall revenue requirement for the 2019-20 test year include:

- O&M Expense, which consists of about 44% of the overall net delivery revenue requirement increase, and is forecast to increase by about $10.316 million (8.2%) over the 2017-18 test year forecast. Restraint measures implemented between 2015-16 and 2017-18 have materially decreased actual spending in each fiscal year compared to the test year forecast.

[1] SaskEnergy 2018 Rate Application, P. 1
[2] Ibid, P. 2
[3] Ibid, P. 2

- Forecast Capital Spending, in which spending on growth and integrity has increased from $7.4 million in 2010 to $53.1 million in 2017-18 and is forecast to increase to $67.6 million by 2019-20. Increases in capital spending impact rates through increased annual expenses regarding depreciation, capital taxes, interest and income.

- Net Earnings, which will increase and account for about 13% of the overall net delivery revenue requirement in the test year compared to the 2017-18 test year, reflecting an increase in rate base.

To minimize the impact of this increase on ratepayers, SaskEnergy indicates that it has been striving to make the most effective use of materials, technology, resources and collaboration with other Crown corporations. SaskEnergy estimates that it has achieved approximately $48 million in savings since 2009 through measures in these areas. For 2018-19, SaskEnergy is targeting a further $4.0 million in annual savings.[4]

Commodity Rate

SaskEnergy buys natural gas on the open market and passes on the cost of natural gas to customers at the same price it pays suppliers, including all expenses. The cost of providing natural gas this coming year is forecasted to be lower than the current rate of 13.87 cents per cubic metre ($3.65/GJ). The proposed interim rate will reduce this rate to 11.36 cents/cubic metre ($2.93/GJ) and then be further reduced to 10.20 cubic metre ($2.63/GJ) effective April 1, 2019, which is an overall decrease of 26.5% from the existing rate.[5]

The interim rate would reduce the balance in the Gas Cost Variance Account (GCVA) of $11.123 million owing to customers from SaskEnergy at April 1, 2019. The final rate would result in a GCVA balance of $3.351 million by March 31, 2020 (assuming a 38.75 MJ/m3 heat value).

Mid Application Update

SaskEnergy provided a mid-application update on November 26, 2018, that compared the original application to the most recent financial forecast as of November 20, 2018.[6] This update was revised on December 3, 2018, with corrected information.

The update reflected an increase in assumed TransGas rates. The original application assumed a 4.0% increase in rates effective April 1, 2019, while the update assumed a 5.5% increase. This new rate increases transportation and storage expense by $0.778 million for the 2019-20 test year.[7]

The update included an increase in depreciation expenses related to transportation vehicles, which was due to an error in the original application which underestimated this expense. This error led to an increase in depreciation expense for the 2019-20 test year by $0.219 million.[8]

There is an overall reduction in tax expense compared to the original application by $0.092 million. This reflects a $0.191 million increase in grants-in-lieu of taxes offset by a $0.283 million reduction in corporate capital tax.

[4] Ibid
[5] InterGroup Report, P. 2-1
[6] Mid-Application Update, P. 1
[7] InterGroup Report, P. 3-39
[8] November 26, 2018 Mid-Application update, P. 6

SaskEnergy also stated that it reviewed the forecast 2019-20 heat value and determined that a higher heat value of 38.75 m^3/MJ (compared to 38.5 m^3/MJ in the original application) is expected for the test year.[9] SaskEnergy prepares its load forecast in GJ and converts into m^3 using a heat value forecast (since the commodity and delivery variable rates are in m^3). The increase in heat value results in a lower load forecast in m^3, which resulted in a $1.0 million reduction in delivery revenues (both existing and proposed rates).

The table below provides a summary comparison of the change in revenue requirement.

Revenue Requirement Comparison: Original Application vs Mid-Application Update ($000s)[10]

Component	Application	Mid-Application Update	*Change*	*% Change*
Operating & Maintenance Expense	136,229	136,457	228	*0.17%*
Transportation and Storage Expense	53,919	54,697	778	*1.44%*
Depreciation Expense	48,186	48,405	219	*0.45%*
Tax Expense	7,362	7,270	(92)	*-1.25%*
Interest Expense	31,450	30,638	(812)	*-2.58%*
Net Earnings	33,459	32,790	(669)	*-2.00%*
Total Delivery Revenue Requirement	**310,605**	**310,257**	**(348)**	***-0.11%***
Other Revenue	(30,411)	(30,411)	0	*0.00%*
Net Delivery Revenue Requirement	**280,194**	**279,846**	***(348)***	***-0.12%***

The net impact of these changes noted above produces an overall revenue shortfall of approximately $1.3 million and a decrease of 0.3% return on equity. The update did not seek changes to the proposed rates in the original application.

[9] InterGroup Report, P. 3-66
[10] Prepared based on Mid-Application Update filed on November 26, 2018 as revised on December 3, 2018.

Introduction

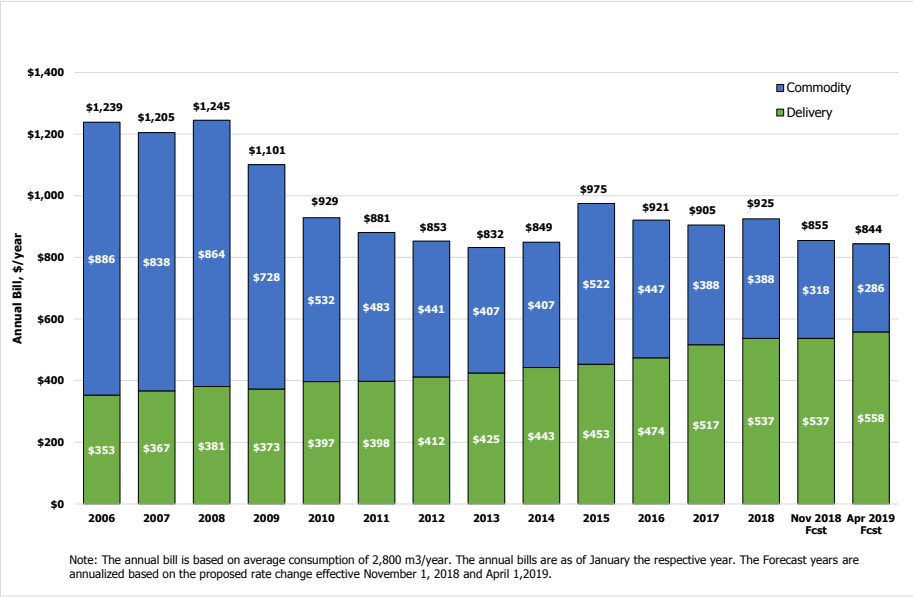
While reviewing the application, the Panel considered the April 1, 2019 test year forecasted results along with past applications, forecast and actual results, and the potential of future applications and rates increases. As the table below indicates, delivery rates have increased every year since 2013, and SaskEnergy has indicated that these rates are expected to continue to increase due to its ongoing integrity and growth capital requirements.

Average Residential Delivery Service Bill Increases[11]

	Sept1, 2013	Sept1, 2014	Jan 1, 2016	Nov 1, 2016	Nov 1, 2017	Apr 1, 2019 [Proposed]
Average Monthly Delivery Service Bill ($/month)	$36.89	$37.77	$39.52	$43.05	$44.76	$46.53
Change in bill ($/Month)	$1.47	$0.89	$1.75	$3.53	$1.71	$1.77
Delivery Service Bill Impact (%)	4.2%	2.4%	4.6%	8.9%	4.0%	4.0%

Recent delivery rates increases have been mitigated to a certain extent by decreases in the commodity rate and commodity portion of residential customer bills (see figure below).

Typical Annual Residential Bills
2006 to 2018 Actual and Forecast for November 2018 and April 2019[12]



Note: The annual bill is based on average consumption of 2,800 m3/year. The annual bills are as of January the respective year. The Forecast years are annualized based on the proposed rate change effective November 1, 2018 and April 1,2019.

Although current natural gas prices have remained low, it is expected that over time natural gas prices will increase and this will drive future commodity rate increases, which would compound the effects of future delivery rate increases.

While reviewing these past applications, forecasts and actual results, the Panel has noted that Information provided

[11] 1st Round Information Request 21(c).
[12] Ibid

by SaskEnergy indicates that recent components of the revenue requirements, such as depreciation expense and interest expense, have been over-forecasted while other components are impacted by ongoing fiscal restraint measures, such as reductions in O&M expenses. The following table outlines the differences between forecast and actual revenue requirements.

Revenue Requirement Comparison: Forecast vs Actuals ($000s)[13]

	2016/17 Test Year [November 1 - October 31]				2017/18 Test Year [November 1 - October 31]			
Component	**Test Year Forecast**	**Actuals**	***Diff.***	***Diff. %***	**Test Year Forecast**	**Actuals**	***Diff.***	***Diff. %***
Operating & Maintenance Expense	124,404	115,078	*(9,326)*	*-7.50%*	125,913	120,672	*(5,241)*	*-4.16%*
Transportation and Storage Expense	51,964	49,879	*(2,085)*	*-4.01%*	52,028	51,630	*(398)*	*-0.76%*
Depreciation Expense	42,130	40,174	*(1,956)*	*-4.64%*	46,207	43,772	*(2,435)*	*-5.27%*
Tax Expense	5,578	5,032	*(545)*	*-9.77%*	5,948	5,914	*(33)*	*-0.55%*
Interest Expense	26,284	24,516	*(1,768)*	*-6.73%*	26,882	25,748	*(1,134)*	*-4.22%*
Net Earnings to get 8.30% ROE	28,302	27,373	*(928)*	*-3.28%*	30,435	29,066	*(1,368)*	*-4.49%*
Total Delivery Revenue Requirement	**278,662**	**262,052**	***(16,608)***	***-5.96%***	**287,412**	**276,802**	***(10,609)***	***-3.69%***
Other Revenue	(24,096)	(29,255)	*(5,158)*	*21.41%*	(24,223)	(40,541)	*(16,317)*	*67.36%*
Net Delivery Revenue Requirement	**254,565**	**232,797**	***(21,768)***	***-8.55%***	**263,189**	**236,260**	***(26,928)***	***-10.23%***

This table shows that the actual net revenue requirement for the 2016-17 test year was about $21.7 million (8.5%) lower than the forecast included in the 2016 Commodity and Delivery Service Rate Application. The actual net revenue requirement for the 2017-18 test year is $26.9 million (10.2%) lower than forecast included in the 2017 Delivery Service Rate Application. The following costs were noted as being lower than forecast for the 2017-18 test year:

- O&M expense was $5.2 million (4.16%) lower than forecast.
- Transportation and storage expense was $0.4 million (0.76%) lower.
- Depreciation expense was $2.435 million (5.27%) lower.
- Interest expense was $1.134 million (4.22%) lower.
- Net earnings required to maintain a 8.3% ROE were $1.369 million (4.5%) lower.
- Other revenues were $16.317 million (67.36%) higher.

The Panel has also noted that SaskEnergy was directed by its shareholder, after the Panel's review and report, to reduce budgeted expenditures to meet specified targets between 2016-17 and 2017-18. The Panel agrees with the consultant's report that this practice has led to materially better actual financial results compared to test year forecasts that were reviewed during the Panel's process. Our consultant commented on this practice:

> "Given past patterns, concern is noted regarding the potential for further direction to be provided relative to the 2019-20 test year subsequent to the Panel's review. Significant O&M or other budget reductions that occur after test year forecasts have been approved create profound fairness issues for ratepayers who do not effectively share in the cost savings. Implementation of further restraint measures after the Panel has filed their report challenges the reasonableness of rates as rates are set but benefits from further restraint measures do not accrue to ratepayers."[14]

[13] Prepared based on Pre-ask #1, 2018 Commodity and Delivery Service Rate Application. The actual results for 2017/18 test year reflect actuals for November 1, 2017 to July 31, 2018 and expected results for August 1 through October 31, 2018. In response to 1st Round Information Request 1 (g), SaskEnergy notes that based on more up to date information the overall net delivery revenue requirement variance between 2017 test year forecast and actual results for 2017-18 is expected in the range of $31.0 million compared to $27 million shown in the table reflecting about $12.6 million lower revenue requirement and about $2 million additional other revenues on top of $40.5 million shown in the table.

[14] InterGroup Report, P. 2-4

2017-18 Fiscal Year Forecast Compared to 2017-18 Fiscal Year Actuals[15]

Component	2017/18 Fiscal Year [April 1 - March 31] Forecast from 2017 Application	Actuals	*Diff.*	*Diff. %*
Operating & Maintenance Expense	124,245	112,680	*(11,565)*	*-9.31%*
Transportation and Storage Expense	50,328	50,342	*14*	*0.03%*
Depreciation Expense	44,031	41,051	*(2,980)*	*-6.77%*
Tax Expense	5,592	5,481	*(110)*	*-1.97%*
Interest Expense	24,823	24,698	*(125)*	*-0.50%*
Total Expenses	**249,019**	**234,252**	*(14,766)*	***-5.93%***
Other Revenues	(23,724)	(38,390)	*(14,665)*	*61.82%*
Net Delivery Revenue Requirement before Net Earnings	**225,294**	**195,862**	***(29,433)***	***-13.06%***
Net Earnings	28,539	70,220	*41,681*	*146.05%*
ROE	8.30%	20.80%	*12.5%*	*150.60%*

As this chart demonstrates, after restraint measures were implemented along with colder-than-normal weather and market forces, there was a significant increase in net earnings in 2017-18 from a forecast of $28.539 million to an actual of $70.220 million and ROE from 8.30% to 20.80%.

ROE has been one of the drivers for recent applications with the long term ROE set at 8.30% by the shareholder (which is considered a given as part of the Panel's review). This rate is consistent with other publicly traded utilities across Canada. A mild winter or an unexpected expense could cause the corporation to realize lower earnings.

The Panel has reviewed SaskEnergy's ability to achieve its target ROE of 8.30%. As demonstrated in the table below, this analysis contains both actual ROE for that year and weather-normalized ROE.

Actual and Weather Normalized Return on Equity[16]

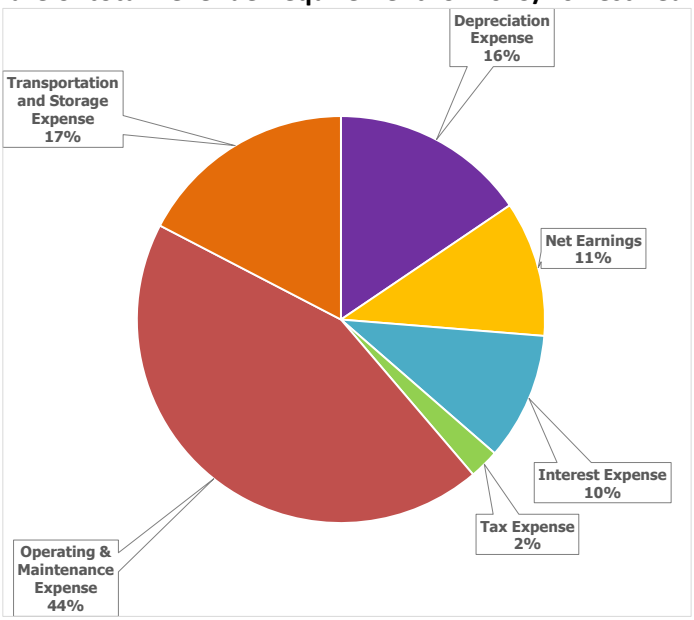
		Distribution Utility		SaskEnergy Consolidated	
		Actual ROE	Weather Normalized ROE	Actual ROE	Weather Normalized ROE
Calendar Years	2006	7.7%	8.0%	14.7%	14.8%
	2007	7.2%	9.5%	15.4%	16.3%
	2008	8.5%	8.2%	12.5%	12.4%
	2009	8.5%	2.4%	13.5%	11.2%
	2010	10.6%	10.6%	10.8%	10.8%
	2011	7.9%	6.3%	13.6%	13.1%
	2012	8.3%	9.7%	11.0%	11.4%
	2013	12.4%	9.0%	11.0%	10.0%
	2014	10.2%	4.5%	6.5%	2.4%
	2015	3.3%	8.0%	12.3%	14.2%
2015/16 Fiscal Year		0.6%	7.0%	11.6%	13.9%
2016/17 Fiscal Year		9.1%	11.4%	8.8%	9.6%
2017/18 Fiscal Year		20.8%	18.6%	12.2%	11.4%
5-year Average		**8.80%**	**9.90%**	**10.3%**	**10.3%**
10-year Average		**9.20%**	**8.70%**	**11.1%**	**10.8%**

[15] InterGroup Report, P. 3-5
[16] Pre-ask #13, 2018 Commodity and Delivery Service Rate Application.

On an actual basis, non-weather normalized ROE for the distribution utility over the last five years average is 8.8%, while the average of weather normalized ROE for the same period was 9.9%. The average for the last ten years indicates non-weather normalized ROE of 9.2%, while the average of weather normalized ROE for the same period was 8.7%. These are all higher than the target ROE of 8.3%. The weather normalized average for SaskEnergy consolidated ROE over the last five years was 10.3% and for the last 10 years was 10.8%.

The main drivers for the revenue requirement in this application are summarized below:

Share of total Revenue Requirement for 2019/20 Test Year[17]



The net revenue requirement of $280.2 million for the 2019-20 test year is forecast to increase by 6.5% over the 2017-18 test year forecast and is $43.9 million (18.5%) higher than actual 2017-18 actuals. The following is specifically noted regarding the main drivers underlying the overall revenue requirement:

- O&M expense makes up about 44% of the overall net delivery revenue requirement increase in the 2019-20 test year over the 2017-18 test year. O&M expense is forecast to increase by about $10.316 million (or 8.2%) over the 2017-18 forecast and is $23.549 million (or 20.8%) higher than the 2017-18 fiscal year actuals.

- SaskEnergy has increased its annual safety and infrastructure renewal investment from $7.0 million in 2008 to about $68 million during the application period, and expects annual investment to continue at these levels into the future. While the capital program is outside of the scope for this review, spending on capital impacts depreciation expense (16%), capital tax expense (2%), and interest expense (10%) which are within the scope of this review and account for a total of 28% of the total net revenue requirement.

- Transportation and storage expense account for 17% of the revenue requirement.

- Net earnings account for the final 11%.

These expenses will be partially offset by $30.4 million in other revenue, which is forecast to decrease by $7.9 million over the 2017-18 fiscal year actual results of $38.4 million.

[17] InterGroup Report, P. 3-2, chart prepared based on Table 3-1.

To help mitigates these rate pressures, SaskEnergy has been implementing a number of different productivity and efficiency measures. For the 2018-19 fiscal year, SaskEnergy has targeted a further $4.0 million in annual efficiency savings. SaskEnergy noted that initiatives planned for 2018-19 are in progress and intended to continue to provide savings to ratepayers in future periods.[18]

[18] 1st Round Information Request, 27(d), 2018 Commodity and Delivery Service Rate Application.

Panel's Recommendations

To the Minister

The Saskatchewan Rate Review Panel, following its review and analysis that included meetings with SaskEnergy management, two rounds of specific information requests, several meetings with its technical consultant, the consultant's independent report, and taking into account public input regarding the application, makes the following recommendations to the Minister:

1. **That the proposed delivery service rate increase of 3.7% effective April 1, 2019 be revised to 3.4%.**

The Panel has identified several factors that impact the proposed delivery rate increase.

The Panel's consultant has indicated that SaskEnergy should use vacancy rate adjustments with the average labour cost of $100,677 (or $4.530 million) for 45 vacant full-time equivalents (FTEs) for 2019-20. This would reduce the total labour cost for the 2019-20 test year by about $0.480 million.

The consultant noted an error in transportation and storage expenses, which led to an increase in the forecast of volumes delivered and increase in the expense of $1.707 million. A recent National Energy Board of Canada decision will reduce the forecasted transportation expense by $0.680 million. These two adjustments have increased the forecast transportation net expense in this category by $1.027 million.

To ensure fairness with all internal transactions with TransGas, the Panel recommends that the cash working capital allowance in rate base be reduced by $2.1 million to reflect revenue lag days from distribution tolls that use 45.6 days. This measure would reduce the revenue requirement by about $0.124 million.

It was noted by the Panel's consultant that changes to reflect net customer funding for future decommissioning be included as no cost of capital which results in a reduction in the revenue requirement of $0.956 million.

The Panel agrees with the consultant's assessment of asset optimization (formerly known as margin on gas marketing) which indicates that revenues in this area are perhaps conservatively forecast and are likely to be much higher than estimated for the test year.

The mid application update noted an overall revenue shortfall of approximately $1.3 million and a decrease of 0.3% ROE. The update did not seek changes to the proposed rates in the original application. The Panel's recommended rates would enable the stakeholder to achieve the revised ROE in the update.

2. **That the Panel's approval for the interim commodity rate decrease effective November 1, 2018 of $3.65/GJ to $2.95/GJ be confirmed.**

The Panel recommended the rate adjustment on November 1, 2018, as interim rate adjustment to allow for a more thorough examination of assumptions and data used to generate a final rate recommendation. After a final review, the Panel now recommends that this interim rate be confirmed.

3. **That the proposed commodity rate effective April 1, 2019 that would see a further decrease to $2.65/GJ be revised to $2.575/GJ to eliminate any outstanding balance in the GVCA.**

The proposed commodity rate effective April 1, 2019 does not fully clear the balance in the GVCA at the end of the test year and would maintain a $3.3 million balance in the account at the end of the test period on March 31, 2020. The purpose of the GCVA is to allow SaskEnergy to recover the cost of gas sold to customers without any mark-up.

Rates are traditionally designed to target a GCVA balance of zero at the end of the test period to minimize the impact of intergenerational equity and fairness.

SaskEnergy indicated it was deviating from this practice due to the current low price of gas, and the increased probability of natural gas prices rising compared to declining further. SaskEnergy also stated that leaving a modest balance in the GVCA would help mitigate a higher commodity rate in the future.

The Panel notes that SaskEnergy has also been able to maintain the same commodity rate for the past two years without the GCVA growing beyond $20 million (either owing to or from customers), and that the corporation has fixed the price on a large portion of its forecasted natural gas purchase for the next five years. If prices remain near current levels, fewer commodity rate changes are anticipated over this period, although even if prices remain constant, a commodity price increase may be required for the 2020-21 year.

The proposed commodity rate in the original application was based on a heat value of 38.50 MJ/m3, which resulted in a final commodity rate of 10.20 cents/cubic metre ($2.65/GJ) effective April 1, 2019. SaskEnergy revised the heat value in the update to 38.75 MJ/m3 which would result in a final commodity rate of 10.20 cents per cubic metre or $2.63 GJ. SaskEnergy has indicated that a commodity rate of $2.575/GJ effective April 1, 2019 would clear the GCVA balance at the end of the 2019-20 test period.[19]

To SaskEnergy

The Panel offers the following recommendations to SaskEnergy arising from its deliberations during this review:

1. **That SaskEnergy use the average base labour cost of $100,677 (or $4.530 million) for the vacancy rate adjustments of 45 vacant full-time equivalents (FTEs) for 2019-20.**

2. **That SaskEnergy in future delivery rate applications provide greater disclosure regarding growth in expenditures related to Labour FTEs and expenditures in External Services. This disclosure should include details regarding the relationship between internal labour and external services cost forecasts, as well as any impacts related to changes in operations (e.g., the transition to hosting services).**

3. **That SaskEnergy carefully review its spending forecasts and to continue to find ways to avoid increases in areas of controllable costs such as professional memberships, dues, training and conferences, as well as discretionary spending areas including sponsorship and donations.**

4. **That SaskEnergy develop a plan to limit future increases in O&M expenses to a measurable target/average cost per customer, such as a percentage related to the annual rate of the Saskatchewan Consumer Price Index.**

5. **That SaskEnergy adjust its revenue requirement to reflect the revisions in transportation and storage expense which is now forecasted to be $55.724 million up from the $54.697 million in the mid-application update.**

6. **That SaskEnergy review its long term policy objective to recovery 75% of costs through the basic monthly charge (BMC) to determine if it is still reasonable.**

7. **That SaskEnergy review the basis for the $20 million quantum as the forecasted metric for the GCVA to determine if it remains appropriate.**

[19] Revised Response to 2nd Round Information Request 4 (a) (Commodity)

8. **That SaskEnergy file the new depreciation study with the Panel along with the corporation's response as soon as reasonably possible.**

9. **That SaskEnergy review the calculations and methodology for the corporate capital tax to the operating division and the holding division of SaskEnergy Incorporated. This review should also consider the effect that IFRS accounting treatment for customer contributions has on corporate tax calculations and update the Panel in the next application.**

10. **That SaskEnergy reduce the cash working capital allowance in rate base by $2.1 million to reflect revenue lag days from distribution tolls that use 45.6 days.**

11. **That SaskEnergy review how future asset removal costs (decommissioning cost, asset retirement obligations or negative salvage) that are collected from customers are reflected in utility rate base. It is recommended that customer provided capital for future decommissioning (accumulated balance of depreciation of decommissioning assets and accretion expenses, less amounts used) be included in the financing portion of rate base as no cost capital.**

12. **That SaskEnergy provide more detailed explanations in future delivery rate applications regarding intercompany allocations, productivity and efficiency measures, capital expenditures, and load forecast.**

13. **That SaskEnergy pursue measures required to shift to billing in energy as soon as possible.**

Analysis and Discussion on the Delivery Service Rate

Operations and Maintenance (O&M)

SaskEnergy's O&M expense includes labour costs, external services, materials and supplies, vehicles, travel, public relations and other costs. These costs are offset through charges to capital, external recoveries, internal recoveries and intercompany allocations to calculate the O&M expense included in the revenue requirement.

Operating & Maintenance Costs by Category[20]

	Calendar Year [Jan 1 to Dec 31]			Fiscal Year [Apr 1 to March 31]				Nov 1 - Oct 31	Fiscal Year [April 1 to March 31]		
Category	2013 Actual	2014 Actual	2015 Actual	2015/2016 Actual	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2017/18 Test Year Forecast from 2017 Application	2019/20 Forecast from Current Application	*Change*	*Percent Change*
Labour	86,912	91,439	89,856	88,882	87,666	88,900	95,258	93,748	100,965	*7,217*	*7.7%*
Pension Costs	357	460	221	216	296	221	201	275	211	*(64)*	*-23.3%*
Charges to Capital	(27,705)	(29,695)	(30,079)	(29,407)	(29,151)	(29,938)	(29,473)	(29,961)	(29,535)	*426*	*-1.4%*
External Services	28,906	35,078	34,408	34,466	33,984	34,156	40,373	41,788	44,109	*2,321*	*5.6%*
External Recoveries	(3,599)	(4,642)	(3,122)	(2,999)	(3,535)	(2,422)	(2,819)	(3,666)	(3,570)	*96*	*-2.6%*
Internal Recoveries	(5,330)	(5,749)	(5,329)	(5,885)	(2,720)	(3,326)	(2,465)	(4,821)	(3,021)	*1,800*	*-37.3%*
Materials and Supplies	7,722	7,940	7,232	7,093	7,509	7,255	8,598	7,658	8,119	*461*	*6.0%*
Energy Costs	569	617	641	640	648	813	764	637	842	*205*	*32.2%*
Vehicles	7,988	8,375	7,728	7,544	6,966	7,015	7,722	7,015	8,038	*1,023*	*14.6%*
Property	4,428	4,832	5,075	4,809	5,328	5,280	6,665	4,242	4,114	*(128)*	*-3.0%*
Computer Costs	4,539	3,875	3,874	3,985	4,449	4,960	5,534	5,452	6,288	*836*	*15.3%*
Sustenance and Transportation	3,696	3,760	3,251	3,194	2,878	2,970	3,546	3,787	3,992	*205*	*5.4%*
Communication	2,224	2,509	2,189	2,149	2,531	2,188	2,585	2,487	2,330	*(157)*	*-6.3%*
Public Relations	3,692	2,594	2,041	1,990	1,898	2,790	2,754	3,041	3,309	*268*	*8.8%*
Fees, Dues and Com. Contr.	2,838	2,974	1,849	1,786	1,659	1,733	1,995	1,974	2,328	*354*	*17.9%*
Misc Corporate Charges	3,099	1,643	4,072	5,536	4,794	881	2,429	3,043	3,494	*451*	*14.8%*
Intercompany Allocations	(8,278)	(9,208)	(8,928)	(9,208)	(9,475)	(10,796)	(13,290)	(10,785)	(15,785)	*(5,000)*	*46.4%*
Total	**112,058**	**116,801**	**114,975**	**114,790**	**115,725**	**112,680**	**130,377**	**125,913**	**136,229**	***10,316***	***8.2%***

As the above table notes, forecast total O&M expenses for the 2019-20 test year is about 8.2% higher than the 2017-18 test year forecast. This includes a 7.7% increase in labour costs and 5.6% increase in external services. The Panel's consultant has indicated that "specifically, the 2019-20 test year forecast is about $23.5 million (or 21% higher than 2017-18 fiscal year actuals.)"[21] This is a concerning trend for the Panel.

LABOUR COSTS

Labour costs represent the largest portion of SaskEnergy's O&M expense (68% for the 2019-20 test year). Actuals for the period from 2013-15 (calendar) and 2015-16 to 2017-18 (fiscal year) show total Distribution Division full-time equivalent (FTE) positions range from 744 in 2017-18 to 797 in 2014. For the 2018-19 fiscal year, SaskEnergy is forecasting an increase in FTE levels to 794, which is 50 FTEs higher than 2017-18 fiscal year actuals. SaskEnergy is forecasting a further increase to 805 FTEs for the 2019-20 test year (please note that a detailed report on labour costs can be found in section 3.1.1 of the consultant's report).

The increase in base and net labour costs reflect an increase in the number of FTEs and an increase in the average labour costs.

[20] Summarized from page 1 of Tab 9 from the 2017 Delivery Service Rate Application, and page 1 of Tab 9 from the 2018 Commodity and Delivery Service Rate Application.
[21] InterGroup Consultants Ltd. Report, P. 3-18

SaskEnergy forecasts 50 FTE additions for the 2018-19 fiscal year and a further 11 additions for 2019-20 test year.[22]

- 32 FTEs (64% of 2018-19 additions) are being added for safety and reliability reasons; and
  20 FTEs over 2018-19 and 2019-20 fiscal years are being added due to contractor conversion for information technology transformation.[23]

- The total FTE forecast of 805 for the 2019-20 test year is much higher compared to recent actuals for the 2017-18 fiscal year (744 FTEs), but is only 1% (or 8 FTEs) higher than 2014 actuals (797 FTEs).[24] SaskEnergy has noted that lower FTEs for 2017-18 reflect vacancy management to meet short term net income targets.[25]

SaskEnergy notes that the cost per contractor is about $199,134[26] compared to about $105,820 for an FTE,[27] and consequently contractor conversions result in approximate savings of $93,000 per FTE conversion (or about $1.5 million savings) "reflected in the contract services category of operating and maintenance expense"[28]. However, the external services category of O&M expense is also forecast to increase by about 18% (or $6.217 million) in 2018-19 over 2017-18 actuals, and further increase by 9.3% ($3.736 million) in 2019-20 over the 2018-19 forecast. This results in a $10 million (or 29%) increase over a two-year period.

Average Labour Costs per Full Time Equivalent[29]

	Calendar Year [Jan 1 to Dec 31]			Fiscal Year [Apr 1 to March 31]				Nov 1 - Oct 31	Fiscal Year [April 1 to March 31]		
	2013 Actuals	2014 Actuals	2015 Actuals	2015/16 Actuals	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2017/18 Test Year Forecast from 2017 Application	2019/20 Forecast from Current Application	*Change*	*Percent Change*
Base Labour Costs ($000s)	67,720	71,293	71,815	71,553	72,027	71,795	76,971	74,896	81,070	*6,174*	*8.2%*
Total Net Labour Costs ($000s)	81,324	85,847	83,933	83,312	81,994	82,681	88,028	86,783	92,208	*5,425*	*6.3%*
Full-Time Equivalents	773	797	782	775	762	744	794	779	805	*26*	*3.3%*
Avg Base Labour / FTE ($/FTE)	87,572	89,472	91,869	92,326	94,519	96,504	96,881	96,102	**100,677**	*4,575*	*4.8%*
Avg Net Labour / FTE ($/FTE)	105,164	107,737	107,370	107,500	107,598	111,137	110,797	111,354	114,509	*3,155*	*2.8%*
Annual Change		2,573	(367)		98	3,539	(340)				
Annual Change, %		2.4%	-0.3%		0.1%	3.3%	-0.3%				

The average net cost per FTE in the 2019-20 test year is about 2.8% higher than the 2017-18 test year. The table above shows a 1.5% average annual increase in average net labour cost over the two year period from 2017-18 fiscal year actuals to 2019-20 test year (increase from $111,137/FTE to $114,509/FTE).

[22] In response to 2nd Round Information Request 3 (b), 2018 Commodity and Delivery Service Rate Application, SaskEnergy notes that the application was based on 11 FTE additions, however, the final budget indicates 17 FTE increase for 2019/20.
[23] 16 out of 50 FTE additions in the 2018/19 fiscal year relate to field employee retention, 24 relate to vacancy management and relate to 10 contractor conversion. All FTE additions for 2019/20 reflect contractor conversions.
[24] There were 760 FTEs net of vacancies for the 2019/20 test year compared to 724 for 2016/17 and 710 for 2017/18; and there was an average of 763 FTEs net of vacancies per year for the period from 2013 through 2015/16 actuals.
[25] For example, see response to 1st Round Information Request 1 (c), (d) and 3 (a).
[26] 2nd Round Information Request 2 (h), 2018 Commodity and Delivery Service Rate Application.
[27] 2nd Round Information Request 3 (j), 2018 Commodity and Delivery Service Rate Application.
[28] 2nd Round Information Request 3 (b), 2018 Commodity and Delivery Service Rate Application.
[29] 1st Round Information Request 3 (i), 2018 Commodity and Delivery Service Rate Application. 2017/18 test year is from page 2, Tab 8 of 2017 Delivery Service Rate Application.

Full-Time Equivalent Vacancies from 2012-15 (calendar) and 2016/17 to 2018/19 (fiscal)[30]

	2013 Actuals	2014 Actuals	2015 Actuals	2015/16 Actuals	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2019/20 Test Year Forecast
Full-Time Equivalents [FTEs]	773	797	782	775	762	744	794	805
Vacant FTEs	16	16	22	22	38	34	40	45
Calculated Vacancy Rate	2.1%	2.0%	2.8%	2.8%	5.0%	4.6%	5.0%	5.6%
Total Labour Cost before Vacancy Rate Adjustment	69,160	72,733	73,795	73,533	75,447	74,855	80,571	85,120
Vacancy Rate Adjustment	1,440	1,440	1,980	1,980	3,420	3,060	3,600	4,050
Total Labour Cost after Vacancy Rate Adjustment	67,720	71,293	71,815	71,553	72,027	71,795	76,971	81,070

The above table shows that for vacancy rate adjustments SaskEnergy used $90,000/FTE ($4.050 million divided by 45 vacant FTEs), while the average base labour cost per FTE is forecast to be $100,677. SaskEnergy notes that "most of the vacancies consistent to historic trend driven by bid lag and employee turnover are in-scope therefore a lower cost per FTE. In addition, field staff retention budgeted each year is difficult in smaller communities as the skill set required is limited in smaller communities."[31]

This table also shows that SaskEnergy used a vacancy rate adjustment of $90,000/FTE for the 2017-18 fiscal year and previous year actuals. This is not consistent with the year-over-year increase in average labour costs as illustrated in this table. Using the average base labour cost of $100,677 (or $4.530 million) for the vacancy rate adjustment for the 45 vacant FTEs for 2019-20 would reduce total labour costs for the 2019-20 test year by about $0.480 million ($4.530 million less $4.050 million).

In light of this information, the Panel recommends that SaskEnergy use the average base labour cost of $100,677 (or $4.530 million) for the vacancy rate adjustments of 45 vacant FTEs for 2019-20. This would reduce the total labour costs for the 2019-20 test year by about $0.480 million.

EXTERNAL SERVICES

SaskEnergy is forecasting an 18% increase ($6.217 million) in external services in 2018-19 over 2017-18 (actuals); and a 9.3% increase ($3.736 million) increase in 2019-20 over 2018-19 (forecast) results, which results in a 29% ($10 million) increase over a two year period. This is a significant increase which is equal to the incremental revenue the corporation is seeking from the 3.7% rate increase in delivery rates.[32]

The increase in external services relate to hosting services ($4.9 million), management of change initiative ($0.7 million), line locating and hydro vac ($0.8 million), and distribution information systems – contractors for change management ($0.4 million).[33]

The mid application update provided by SaskEnergy indicated that O&M expense increases by about $0.228 million (or 2%) compared to the original application. Hosting costs for Geographical Information Systems (part of external services) was cited as the main reason for the change in operations costs in the update. This includes using third party data center facilities to host company-owned hardware, vendor provided support for applications, and vendor hardware and software support.[34]

[30] Prepared based on information provided in Pre-Ask #4, 2018 Commodity and Delivery Service Rate Application.
[31] 1st Round Information Request 3 (m), 2018 Commodity and Delivery Service Rate Application.
[32] InterGroup Consultants Report, P. 21-3
[33] Ibid
[34] 2nd Round Information Request 2 (e), 2018 Commodity and Delivery Service Rate Application.

SaskEnergy indicates that the move towards hosting services will provide for better workflow and decision-making that ensures that trusted information can be made securely available to staff, customers and stakeholders through integrated business processes and systems. SaskEnergy notes that the primary benefits to this approach are reliability, security and maintenance of software solutions that can be leveraged to make good business decisions and provide an appropriate level of customer service.[35]

The information provided by SaskEnergy indicates that hosting costs will be $5 million higher in 2019-20. An example provided by the corporation shows that the annual cost for hosting the ClickSoftware application at SaskTel is $441,528 for the 2018-19 fiscal year compared to SaskEnergy's 2017-18 internal costs of $374,000 for Software Maintenance and $12,000 for contract analyst support, which is a 15% higher cost. This example suggests that SaskEnergy may be paying a 15% premium for "reliability, security and maintenance of software solutions" for this specific application. This example applied more broadly would suggest that the added cost of $5 million to replace work performed internally would be expected to reduce internal costs by approximately $4.25 million ($5 million less 15%). However, the actual costs for other applications and extent to which there is any added premium for other applications is not known.

Related cost reductions that would offset the increase in hosting services are neither specified nor apparent in the 2019-20 test year. As such, the Panel recommends that SaskEnergy in future delivery rate applications provide greater disclosure regarding growth in expenditures related to labour FTEs and expenditures in External Services. This disclosure should include details regarding the relationship between internal labour and external services cost forecasts, as well as any impacts related to changes in operations (e.g., the transition to hosting services).

COMMUNICATIONS, PUBLIC RELATIONS, FEES, DUES AND COMMUNITY COSTS

There has been a notable increase in communications, public relations, fees, dues and community related costs in the 2018-19 and 2019-20 fiscal years, which are related to the implementation of restraint measures in 2016-17 and 2018-19 fiscal years that reduced expenditures in certain cost areas.

Total Safety and Awareness Average Cost Per Customer[36]

	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2019/20 Forecast
Total Safety and Awareness	794,754	794,594	915,179	1,167,546
Average # of Customers	390,886	394,592	398,434	402,069
Total Cost Per Customer	2.03	2.01	2.30	2.90

This table shows total safety and awareness spending per customer for 2018-19 and 2019-20 compared to 2016-17 and 2017-18 actuals. The actual average cost per customer was at the $2.03 and $2.01 level for 2016-17 and 2017-18 and is forecast to increase to $2.90 by the 2019-20 fiscal year. SaskEnergy has indicated there is "an increased focus on regulatory compliance which results in additional costs to safety and awareness policies/programs"[37]; however, no specific examples were provided.

Over the last several years, due to the implementation of restraint measures, SaskEnergy was able to reduce costs related to professional memberships and dues as well as training and conferences. Since there is ongoing pressure on delivery service rates due to ongoing safety and integrity spending requirements, the Panel recommends that

[35] 1st Round Information Request 6 (a), 2018 Commodity and Delivery Service Rate Application.
[36] 2nd Round Information Request 2 (d), 2018 Commodity and Delivery Service Rate Application.
[37] 2nd Round Information Request 2 (c), 2018 Commodity and Delivery Service Rate Application

SaskEnergy carefully review its spending forecasts and continue to find ways to avoid increases in areas of controllable costs such as professional memberships, dues, training and conferences, as well as discretionary spending areas including sponsorship and donations**.**

LINKING O&M TO INFLATION

It should be noted that the Panel recommended to SaskPower in 2016 and 2017 that the corporation limit O&M costs on a per customer basis to half of the increase in the Saskatchewan Consumer Price Index as a reasonable stretch target to achieve on a go-forward basis. Since that time SaskPower has been able to limit increases to less than 1%.

The following chart shows the O&M cost per average number of customers for SaskEnergy:

Operating & Maintenance Cost per Average Number of Customer[38]

	Calendar Year [Jan 1 to Dec 31]			Fiscal Year [Apr 1 to March 31]				Nov 1 - Oct 31	Fiscal Year [April 1 to March 31]		
	2013 Actual	2014 Actual	2015 Actual	2015/16 Actual	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2017/18 Test Year Forecast from 2017 Application	2019/20 Forecast from Current Application	*Change*	*Percent Change*
O&M Expense ($000s)	112,058	116,801	114,975	114,790	115,725	112,680	130,377	125,913	136,229	*10,316*	*8.2%*
Avg. Number of Customers	366,882	377,102	382,666	386,886	390,886	394,592	398,434	394,548	402,069	*7,521*	*1.9%*
O&M per Customer ($/Customer)	305.4	309.7	300.5	296.7	296.1	285.6	327.2	319.1	338.8	*19.7*	*6.2%*
Annual Change		4	(9)		(1)	(10)	42				
Annual Change, %		1.4%	-3.0%		-0.2%	-3.5%	14.6%				

This table indicates that the 2018-19 fiscal year forecast average O&M cost per customer increases by 14.6% ($285.6 to $327.2) over the 2017-18 fiscal year; and the 2019-20 fiscal year forecast shows a 3.5% increase over the 2018-19 fiscal year forecast. There is also a 6.2% increase in average O&M costs per customer in the 2019-20 test year forecast over the 2017-18 test year forecast. In contrast, from 2015 to 2017-18, actual year-over-year changes in average O&M cost per customer were lower than each previous year.

Due to escalating costs in O&M expenses, the Panel recommends that SaskEnergy develop a plan to limit future increases in O&M expenses to a measurable target, such as a percentage related to the annual rate of the Saskatchewan Consumer Price Index.

Transportation and Storage

Delivery transportation service is provided by TransGas Limited (TransGas), a wholly owned subsidiary of SaskEnergy.[39] TransGas also owns and operates a non-regulated natural gas storage business integrated with the transmission pipeline system. SaskEnergy contracts with TransGas for both transportation and storage services on behalf of its delivery customers. Delivery transportation expense includes the cost of transporting natural gas from the TransGas Energy Pool to SaskEnergy's distribution system pressure regulating stations.

[38] Summarized from page 3 of Tab 9 from the 2017 Delivery Service Rate Application, and page 3 of Tab 9 from the 2018 Commodity and Delivery Service Rate Application.
[39] Page 7 of 2018 Commodity and Delivery Service Rate Application.

Transportation and storage expense make up approximately 17% of the total delivery revenue requirement in the 2019-20 test year, and is the second largest component of the revenue requirement after O&M expenses. For the 2019-20 test year, transportation and storage expense in the application was forecasted to be $53.919 million, which was $1.891 million higher compared to the 2017-18 test year actual financial results.

The forecast expense for the 2018-19 fiscal year is about $2.367 million (or 4.7%) higher compared to 2017-18 actuals, reflecting an increase in transportation and storage rates effective May 1, 2018.[40]

SaskEnergy is forecasting a further increase over 2018-19 forecast in the 2019-20 test year of $1.210 million (or 2.3%). SaskEnergy noted that the forecast increase for the 2019-20 test year includes a transportation and storage rate increase assumption of 4% effective April 1, 2019.[41]

The table below provides a summary of the year-to-year changes in the transportation and storage expense, including a forecast for the 2019-20 test year compared to the 2017-18 test year.

Comparison of Transportation and Storage Expense[42]

	Calendar Year [Jan 1 to Dec 31]			Fiscal Year [Apr 1 to March 31]				Nov 1 - Oct 31	Fiscal Year [April 1 to March 31]		
Category	2013 Actuals	2014 Actuals	2015 Actuals	2015/16 Actuals	2016/17 Actual	2017/18 Actual	2018/19 Forecast	Test Year Forecast from 2017 Application	2019/20 Forecast from Current Application	*Change*	*Percent Change*
Transportation Costs	28,580	30,037	31,282	31,516	31,821	31,986	32,665	33,091	33,696	*605*	*1.8%*
Storage Costs	14,777	15,830	17,265	17,569	18,355	18,355	20,044	18,937	20,223	*1,286*	*6.8%*
Total	**43,357**	**45,867**	**48,547**	**49,085**	**50,176**	**50,342**	**52,709**	**52,028**	**53,919**	***1,891***	***3.6%***
Transportation Contracted Demand (GJ/day)	575,020	585,000	590,000	595,000	600,000	600,000	605,000	600,000	605,000	*5,000*	*0.8%*
Contracted Firm Deliverability (GJ/day)	382,838	383,244	391,478	393,217	393,217	393,217	393,217	394,194	393,217	*(977)*	*-0.2%*
Contract Storage Volume (PJs)	20.9	21.8	23.6	23.4	23.4	23.4	23.4	23.4	23.4	*0.0*	*0.0%*
Annual Change in Total Costs		2,510	2,680		1,091	166	2,367				
Annual Change, %		5.8%	5.8%		2.2%	0.3%	4.7%				

During the Panel's process of discovery and clarification, SaskEnergy provided an updated financial forecast which reflected an increase in assumed TransGas rates for 2019. The original application assumed a 4.0% increase in TransGas rates effective April 1, 2019, while the update assumes a 5.5% increase in TransGas rates effective April 1, 2019.[43] Based on the mid-application update, this further increased transportation and storage forecasted expense by $0.778 million for the 2019-20 test year. The update does not indicate a specific rationale for the revised TransGas rate increase assumption.

In response to interrogatories, SaskEnergy indicated that transportation expense for the 2019-20 test year has been underestimated due to an error in the calculation of contracted demand for transmission for April 2019 to October 2019.[44] The Panel's consultant estimates that this results in an approximate $1.7 million underestimation of transportation expense for the test year,[45] which SaskEnergy has since confirmed.

[40] Page 18 and Pre-ask #7. 2018 Commodity and Delivery Service Rate Application.
[41] 1st Round Information Request 9 (a), 2018 Commodity and Delivery Service Rate Application.
[42] Schedule 4.1 from the 2018 Commodity and Delivery Service Rate Application, Schedule 1.1 from the 2017 Delivery Service Rate Application. 2015 Contracted Firm Deliverability (GJ/day) is corrected as per 1st Round Information Request 9 (b), 2018 Commodity and Delivery Service Rate Application.
[43] November 26, 2018 Mid-Application update, page 4.
[44] Per the response to 2nd Round Information Request 7(b) the calculation of contracted demand for transportation used 555,000 GJ/day instead of 605,000 GJ/day. It is estimated by the Consultant that this results in an underestimating of transportation expense for 2019/20 test year of $1.7 million.
[45] Estimated based on transportation demand rate at $4.9467/GJ and 50,000 MJ/day/month for April through October of 2019 [605,000 – 555,000].

The Panel recognizes that the overall rate increase being sought is not being adjusted to take this underestimation into consideration. The financial result of the TransGas forecasted rate change from 4% to 5.5% ($778,000) together with the above underestimation of transportation expense the total transportation and storage expense is now forecasted total to be $56.397 million, or $ 2.478 million greater than the original application forecast.

After the consultant's final report was submitted, the Panel became aware of a National Energy Board (NEB) of Canada decision dated December 13, 2018, which will impact both TransGas and SaskEnergy transportation expense of moving natural gas from Alberta to Saskatchewan in the 2018-2020 time frame covered by this application. The complete decision is available at
https://docs2.neb-one.gc.ca/ll-eng/llisapi.dll?func=ll&objId=3723583&objaction=download&viewType=1

TransCanada submitted that, in the *RH-001-2014 Reasons for Decision*, the NEB approved TransCanada's proposed treatment of the Long Term Adjustment Account (LTAA) defined in the settlement as an adjustment account to capture all variances between the actual and forecast costs and revenues during the period 2015-20, net of incentive mechanism adjustments. TransCanada submitted that the LTAA balance has grown to approximately $1.1 billion, the increase largely due to incremental billing determinants (BDs) and corresponding revenue from 2015-17.

In order to better align with established tolling principles, the NEB has decided that 100 per cent of the LTAA be returned to shippers, which includes TransGas and indirectly SaskEnergy, in the 2018-20 period using the over-collection allocation method as proposed by the Canadian Association of Petroleum Producers (CAPP) as detailed in its submission during the NEB's hearing process. The NEB directed TransCanada to submit a compliance filing to dispose of 100 per cent of the LTAA in the 2018-20 period and to allocate the LTAA amount to each mainline segment using the over-collection method, as proposed by CAPP in this proceeding.

The financial impact on transportation expense has been forecasted to reduce the mainline rate impact on the LDC by reducing transportation expense by $680,000 and the total transportation expense is now forecasted to be $35.363 million including the $ 1.707 million impact of the corrected contract volumes.

It is understood that TransGas transportation and storage rates are subject to Provincial Cabinet approval, and outside the scope of the Panel's Terms of Reference. However, in light of the environment of ongoing expected rate increases related to spending on safety and integrity on the TransGas overall system, and in order for the Panel to be able to assess the reasonableness of all elements of the revenue requirement, there is a need to better understand these matters as they impact SaskEnergy's revenue requirement and rates.

As a result, the Panel recommends the net revenue requirement be adjusted to reflect both of these adjustments to the total transportation and storage expense which is now forecasted to be $55.724 million up from the $54.697 million in the mid-application update.

Other Revenue

SaskEnergy earns other revenue from a variety of sources including connect fees, asset optimization (previously gas marketing margins), distribution tolls and other miscellaneous revenues. The table below summarizes actual other revenue from 2013-15 calendar years, 2015-16 to 2017-18 fiscal years, forecasts for 2018-19 and 2019-20 fiscal years, as well as 2017-18 test year forecast from the previous application.

Other Revenue ($000s)[46]

	Calendar Year [Jan 1 to Dec 31]			Fiscal Year [Apr 1 to March 31]				Nov 1 - Oct 31	Fiscal Year [April 1 to March 31]		
	2013 Actuals	2014 Actuals	2015 Actuals	2015/16 Actuals	2016/17 Actual	2017/18 Actual	2018/19 Forecast	2017/18 Test Year Forecast from 2017 Application	2019/20 Forecast from Current Application	*Change*	*Percent Change*
Connect Fees	2,190	2,164	2,072	2,058	2,034	1,983	2,094	1,900	2,050	*150*	*7.9%*
Asset Optimization	5,229	746	4,052	3,919	5,644	16,197	11,799	2,100	5,913	*3,813*	*181.6%*
Late Payment Charges	540	1,235	1,191	1,186	1,132	1,112	1,326	922	1,200	*278*	*30.2%*
Customer Financing	81	92	99	76	98	115	90	61	64	*3*	*4.9%*
Miscellaneous Revenue	941	1,058	476	413	520	568	464	384	575	*191*	*49.7%*
Distribution Tolls	13,196	14,658	16,420	16,557	16,264	18,414	19,333	18,856	20,609	*1,753*	*9.3%*
Total	**22,178**	**19,954**	**24,311**	**24,209**	**25,692**	**38,390**	**35,106**	**24,223**	**30,411**	***6,189***	***25.6%***
Annual Change		(2,224)	4,357		1,483	12,698	(3,284)				
Annual Change, %		-10.0%	21.8%		6.1%	49.4%	-8.6%				

Forecast other revenues for the 2019-20 test year are $30.411 million, which is $ 7.979 million less compared to the 2017-18 test year actual results. The rationale behind this include increases in connect fees, late payment charges, distribution tolls and other miscellaneous revenues. However, the largest impact is felt in asset optimization revenue forecast reduction.

The forecast revenue of $5.913 million for 2019-20 test year is lower than the most recent actual revenue of $16.197 million in 2017-18. SaskEnergy notes that pipeline capacity constraints at the Alberta/Saskatchewan border have resulted in "unprecedented pricing differentials to the AECO price for downstream gas". This premium has continued over the summer period and has allowed SaskEnergy to realize profit margins on its asset optimization activities because of the significant amount of under-utilized transportation capacity that SaskEnergy has available for optimization during the summer months. SaskEnergy also notes that "this pipeline constraint issue at the Alberta/Saskatchewan border is expected to continue for at least two or three more years but diminishing slightly each year"[47] and the "magnitude of asset optimization revenues is dependent on the alignment of underutilized assets/capacity with market pricing opportunities, and is therefore difficult to forecast."[48]

The Panel recognizes that revenues from asset optimization are difficult to forecast and could be highly variable from year to year. As SaskEnergy notes the "magnitude of asset optimization revenues is dependent on the alignment of underutilized assets/capacity with market pricing opportunities, and is therefore difficult to forecast."[49] However, experience in recent years shows that forecast revenues have been underestimated.[50]Where there are variances between forecast and actual other revenues sources, SaskEnergy bears the risk (or benefit) to its net income. The above table shows year-over-year fluctuations in asset optimization revenues. Although it is difficult to forecast revenues from this source, the ongoing impact of over or under-forecasting these revenues can be material. During the review of the 2017 application, SaskEnergy forecast revenues from this source at $2.102 million while actual revenues were $16.197 million, which contributed to the very high net income realized for the 2017-18 fiscal year.

SaskEnergy notes that asset optimization revenues are expected to be higher than normal for the next few years but

[46] Schedule 4.7 from the 2018 Commodity and Delivery Service Rate Application and Schedule 1.7 from the 2017 Delivery Service Rate Application.
[47] 1st Round Information Request 13(a), 2018 Commodity and Delivery Service Rate Application.
[48] 1st Round Information Request 13(e), 2018 Commodity and Delivery Service Rate Application.
[49] 1st Round Information Request 13(e), 2018 Commodity and Delivery Service Rate Application.
[50] For example, in the 2016 Commodity and Delivery Service Rate Application, the forecast revenues from this source were $2.081 million for the 2016 calendar year and $1.531 million for the 2017 calendar year [the forecast assumed to be included as the base for developing the 2016/17 test year forecast of $1.581 million which was from November 1, 2016 through October 31, 2017], while the actual revenues for the 2016/17 fiscal year were at $5.644 million. Similarly, in the 2017 Delivery Service Rate Application the forecast revenues from this source for the 2017/18 fiscal year were at $2.102 million, while the actuals for the same period were $16.197 million. See Schedule 4.7 from the 2016 Commodity and Delivery Rate Application; Schedule 1.7 from the 2017 Delivery Rate Application; and Schedule 4.7 from the 2018 Commodity and Delivery Rate Application.

will diminish slightly each year. However, the 2019-20 test year forecast shows a 63% reduction in revenues from this source ($16.197 million in 2017-18 to $11.799 million in 2018-19 to $5.913 million in 2019-20). The Panel's consultant has indicated that this forecast may be overly conservative. This analysis is based on the following:

- SaskEnergy increased firm transportation capacity from Alberta from 150,000 GJ/day to 170,000 GJs/day effective November 1, 2018,[51] and "SaskEnergy contracted for an additional 10,000 GJs/day of firm transportation from Alberta beginning in November of 2019, and another 10,000 GJs/day effective November 1, 2020."[52]

- SaskEnergy notes that "in October of 2017, TransCanada Pipelines announced that their firm transportation capacity to move gas out of Alberta was fully subscribed."[53] SaskEnergy also noted that a transformational change occurred regarding natural gas transportation in the fall of 2018, when the National Energy Board approved a long-term fixed price contract from Empress (Alberta/Saskatchewan border) to Dawn (Ontario) on TransCanada's mainline and this event "resulted in transportation capacity from Alberta to the Saskatchewan border becoming fully contracted" and with the system constrained, "the Saskatchewan price differential to AECO has been higher and much more volatile, resulting in natural gas prices in Saskatchewan trading between $0.09/GJ and $2.00/GJ higher than the AECO price."[54]

- "The design level for system delivery capacity used at SaskEnergy means there is only a 5% chance that the weather would be colder than the design level."[55]

- SaskEnergy noted that the pipeline constraint issue at the Alberta/Saskatchewan border is "expected to continue for at least two or three more years, but diminishing slightly each year. The current market price differentials to AECO for gas downstream of the constraint continues to be very strong, but decreases each forward year. Asset optimization revenues are expected to be higher than normal for these next few years, but potentially less than the current year because of these decreasing price differentials each year."[56]

- SaskEnergy noted that for the 2017-18 fiscal year approximately $9.0 million in asset optimization revenues were generated during the summer and $7.2 million during the winter months; and for 2018-19, the split is projected to be approximately $12 million during the summer months and $1 million during the winter months.[57] This supports the fact that in the recent year asset optimization revenues were mostly in summer months, which is not impacted by weather. SaskEnergy also notes that expected revenues from this source for the 2018-19 fiscal year are forecasted to be $13.0 million, about $1.2 million higher than the forecast included in the application. [58]

In view of this analysis, the Panel concludes that it appears reasonable to assume that revenues from asset optimization are conservatively forecast and may be much higher than estimated for the test year.

Basic Monthly Charge (BMC) Policy

SaskEnergy has an objective of recovering 75% of customer related costs through the fixed basic monthly charge (BMC). In this application, SaskEnergy proposed to move away from that target since "comments from customers and

[51] Page 11, 2018 Commodity and Delivery Service Rate Application.
[52] 1st Round Information Request 2 (g) iii) [Commodity], 2018 Commodity and Delivery Service Rate Application.
[53] Page 10, 2018 Commodity and Delivery Service Rate Application.
[54] 2018-19 First Quarter Report, page 3. Tab 26, 2018 Commodity and Delivery Service Rate Application.
[55] Page 12, 2018 Commodity and Delivery Service Rate Application.
[56] 1st Round Information Request 13 (e), 2018 Commodity and Delivery Service Rate Application.
[57] 2nd Round Information Request 11 (b), 2018 Commodity and Delivery Service Rate Application.
[58] 2nd Round Information Request 11 (b), 2018 Commodity and Delivery Service Rate Application.

the public indicated a resistance to further increase in the BMC" leading to an increase in the volumetric charge to recover revenue shortfall. As well, maintaining the BMC at the 75% target would require all rate increases be shifted to the BMC rather than volumetric charge. Conversely, SaskEnergy notes that reducing the amount recovered through the BMC would result in more income variability for the utility.

In light of these circumstances, the Panel recommends that SaskEnergy review its long term policy objective to recovery 75% of costs through the BMC to determine if it is still reasonable.

While conducting this review, SaskEnergy should consider the following:

- It is understood that the majority portion of the delivery service costs are fixed and SaskEnergy is entitled to recover those costs from its customers. BMC provides a more stable revenue stream for SaskEnergy compared to the volumetric charge, which is dependent on weather conditions.

- Customer acceptability – as SaskEnergy indicates that comments from customers and the public indicated a resistance to further increases in the BMC.

- The risk of income variability.

- Peer utility comparisons – a comparison of peer utilities regarding the portion of the revenues collected through fixed rates versus variable rates, as well as comparison of monthly charges by customer class.

Gas Cost Variance (GCVA) Threshold

SaskEnergy monitors commodity risk by reviewing future potential changes to the GCVA. The corporation typically reviews and adjusts its commodity rate once or twice a year, but if the GCVA is projected to grow to $20 million or more (surplus or deficit) before the semi-annual review process, it may bring forward a recommendation to its board of directors prior to the next scheduled commodity rate adjustment.

SaskEnergy indicates that the +/- $20 million quantum is a forecasted metric. This means that rather than wait for the GCVA to reach $20 million before bringing forward an application, the impact that future natural gas prices could have on the GCVA are monitored and if the forecasted GCVA balance is projected to exceed the threshold before April 1 or November 1, an application process is triggered. This typically allows sufficient time to complete the governance process and the Panel review process before the GCVA exceeds the $20 million threshold.[59]

Most peer utilities have automatic rate adjustments that occur monthly or quarterly, while SaskEnergy adjusts its rate on a less frequent basis. Since 2012 it has adjusted its commodity rate on average of about 20 months between applications. Although this approach promotes rate stability, which is valued by SaskEnergy's customers, it also raises concerns about intergenerational fairness.

SaskEnergy provides frequent updates to the Panel on the balances of the GCVA, but these updates do not trigger a commodity rate application. The Panel believes there is merit in developing a formalized policy that includes a framework for more regular, automatic adjustments to commodity rates to ensure that large balances do not accumulate and to mitigate concerns related to intergenerational equity.

As such, the Panel recommends that SaskEnergy review the basis for the $20 million quantum as the forecasted metric for the GCVA to determine if it remains appropriate.

[59] Commodity 2nd Round Information Request 1 (a). SaskEnergy notes that on occasion the balance has exceeded $20 million – however, this is typically due to unforeseen delays in the governance process.

Depreciation Expense

Depreciation expense in the 2019-20 test year is forecast to increase by 4.3% (or $1.979 million) over the 2017-18 test year. This is about 9% of the total increase in revenue requirement in 2019-20 over the 2017-18 test year.

The revised mid-application update included an increase in depreciation expense related to transportation vehicles due to an error in the original application that underestimated depreciation expense for this asset category. This increased depreciation expense for the 2019-20 test year by $0.219 million.[60]

There has been an 8% annual average increase in depreciation expense since the last depreciation study was conducted in 2013. This expense is forecast to continue, which puts pressure on customer rates in the near term and likely over the longer term.

The Panel's consultant has noted that about 64% of total net depreciation expense (net of amortization of customer contributions) relates to distribution plant. New improvements and infrastructure may have longer service lives compared to existing assets that are being replaced.[61] In this regard, extending service lives through ongoing system integrity programs may reduce annual depreciation expense related to new capital investments; and ensuring depreciation rates match the useful lives of new or improved assets in service may help to mitigate related rate impacts.

SaskEnergy has contracted an external consultant to complete a new depreciation study by March 31, 2019.[62]

The Panel has determined that the depreciation expense for the test year appears to be reasonable, but recommends that SaskEnergy file the new depreciation study with the Panel along with the corporation's response as soon as reasonably possible.

Tax Expense

SaskEnergy's tax expense consists of a corporate capital tax and grants in lieu of taxes. SaskEnergy Incorporated pays a corporate capital tax to the Province of Saskatchewan which is calculated at 0.6% of capital invested in excess of $10 million, and in accordance with the formula, and deductions and allowances as prescribed by *The Saskatchewan Corporation Capital Tax Act.*[63] It also pays grants in lieu of taxes where it purchases existing infrastructure that had a previous property tax obligation. In the 2018-19 Provincial Budget, the province expanded the grants-in-lieu program to now include all owned, non-linear real estate assets.[64] The increase in tax expense in the 2019-20 test year over 2017-18 test year is about 6% of the total revenue requirement increase.

The consultant has a detailed report on capital tax in Section 3.4 of its report. Based upon this analysis, the Panel noted that the 2019-20 fiscal year corporate capital tax calculation includes capital beyond those attributable to the Distribution Division, such as SaskEnergy Incorporated Holdings division debt, equity and equity advances.[65] The majority of Taxable Paid Up Capital included in the corporate tax calculation is from Loans and Advances. More than half of the Loans and Advances are for Holdco Equity Advances and SaskEnergy Incorporated Subsidiary Debt. Only $765 million of the total $1,576 million or 48.5% of Loans and Advances in the 2019-20 fiscal year forecast relates to the Distribution Division. SaskEnergy also notes that the "Distribution Division administers the total debt on behalf of all subsidiary companies of SaskEnergy Incorporated" and "within the corporate capital tax calculation, there is a considerable investment allowance and a standard exemption provided to the Distribution Division to offset the debt

[60] November 26, 2018 Mid-Application update, page 6.
[61] 1st Round Information Request 9(c) and (d) 2016 Commodity and Delivery Service Rate Application.
[62] 2nd Round Information Request 10 (a), 2017 Delivery Service Rate Application.
[63] Page 28, 2018 Commodity and Delivery Service Rate Application
[64] Ibid
[65] 1st Round Information Request 12 (e), 2018 Commodity and Delivery Service Rate Application

used to finance all of SaskEnergy Incorporated's subsidiary companies."[66] Based upon the consultant's analysis, the corporate tax calculated for the Distribution Division would be $5.807 million compared to the $6.987 million total corporate tax. This would lead to a reduction in the revenue requirement of $1.180 million.

The consultant also noted that under International Financial Reporting Standards (IFRS), SaskEnergy recognizes customer contributions as revenues in the year received (recognized as income), while for regulatory purposes, customer contributions are included as an offset to plant in-service (with relevant adjustments to the plant in-service, accumulated depreciation and depreciation expense).

Due to the uncertainties regarding tax expense, the Panel recommends that SaskEnergy review the calculations and methodology for allocating the Corporation Capital Tax to the operating division and the Holding division of SaskEnergy Incorporated. Included in this review would be consideration of the effect that IFRS accounting treatment for customer contributions has on corporate tax calculations (which SaskEnergy estimates to be about $0.560 million) and update the Panel before the next application.

Rate Base

DISTRIBUTION TOLL LAG DAYS

Lag days for distribution toll revenues are much higher compared to the lag days for other revenue sources, as well as compared to the transportation and storage expense (82.90 days distribution toll revenues compared to 40 days for the other rate revenues, and 45.6 days for transportation and storage expenses).[67] In 2017 SaskEnergy reported that these lag days are longer compared to the lag for rate revenues due to TransGas' "processes for consolidating and verifying volumes from metres across the province" and the "lack of automation and reconciliations required for verification and billing necessitate the long lag."

SaskEnergy has further indicated that "82.90 days was determined based on historic trend of actual cash receipts compared to actual revenue earned" and using 45.6 days (consistent with transportation and storage expense lag days) would result in approximately $2.1 million reduction in the cash working capital allowance.[68] This would, in turn, reduce the revenue requirement by about $0.124 million.[69]

SaskEnergy's information indicates that the average lag days for the distribution toll revenues for the last five years has ranged between 63 and 71 days and the "terms within the contract state that the revenues will be invoiced on the 20th day of the month following a payment term within 10 days."[70] As a result, there does not appear to be a basis for using 82.90 lag days. The Panel believes that the cash working capital allowance in the rate base can be reduced by $2.1 million to reflect revenue lag days from distribution tolls that use 45.6 days, thereby reducing the revenue requirement.

To ensure fairness with all internal transactions with its subsidiary, the Panel recommends that SaskEnergy reduce the cash working capital allowance in rate base by $2.1 million to reflect revenue lag days from distribution tolls that use 45.6 days. This would reduce the revenue requirement by about $0.124 million.

[66] 2nd Round Information Request 11 (a), 2018 Commodity and Delivery Service Rate Application
[67] InterGroup Consultants Ltd. Report, P. 3-72
[68] 1st Round Information Request Delivery 18 (c), 2018 Commodity and Delivery Service Rate Application
[69] $2.1 million reduction in base rate times 5.9% return on rate base as per Revised Tab 14, page 1 (revised for Mid-Application Update).
[70] 2nd Round Information Request Delivery 15 (a) and (b), 2018 Commodity Delivery Service Rate Application

CAPITAL STRUCTURE AND RATE BASE

Since 2013, SaskEnergy has been collecting funds from customers for future decommissioning as part of rates. By the end of 2019-20 SaskEnergy is forecasting to have about $21 million of unused customer provided capital (collected as part of rates at $42.9 million less $21.6 forecast to be used by end of test year). The collected funds are being used by SaskEnergy to fund operational and capital projects (i.e., allowing SaskEnergy to avoid additional borrowing and use its own funds to fund some projects). The Panel has reviewed utilities in other jurisdictions that include a credit in rate base to reflect customer provided capital for future cost of removal. SaskEnergy included a similar rate base offset in pre-2013 rate applications before transitioning to IFRS.

The table below provides an illustrative example which shows the impact of recognizing customer provided funds collected for future decommissioning[71] by including these amounts as no cost capital in financing rate base. This table includes customer-provided capital as a reduction in the debt portion of rate base (as SaskEnergy capitalization is based on 37% deemed equity). This reduces the debt portion of rate base and results in an approximate $0.955 million reduction in revenue requirement.

Impact of Recognizing Net Customer Provided Funds for Future Cost of Removal[72]

Line No		Total Rate Base	Capital Ratio	ROE/Cost of Debt	Total Return on Rate Base
		A	B	C	D=A*C
	As Filed By SaskEnergy				
1	Deemed Equity Portion	395,056	37.0%	8.14%	32,148
2=3-1	Deemed Debt Portion	672,663	63.0%	4.55%	30,638
3	**Total Rate Base**	**1,067,719**		**5.88%**	**62,786**
	Illustrative Option				
1	Deemed Equity Portion	395,056	37.0%	8.14%	32,148
2=4-1-3	Deemed Debt Portion	651,663	61.0%	4.55%	29,682
3	Net Customer Provided Funds for Future Cost of Removal	21,000	2.0%	0.00%	0
4	**Total Rate Base**	**1,067,719**		**5.79%**	**61,830**

Based on review of SaskEnergy's approach prior to 2013, and approaches used in other jurisdictions, the Panel agrees with consultant's analysis that there are material concerns regarding the current treatment of customer provided capital for future decommissioning in rate base financing. As such, the Panel recommends that SaskEnergy review how future asset removal costs (decommissioning cost, asset retirement obligations or negative salvage) are collected from customers and how pre-collected funds are reflected in utility rate base in other jurisdictions. It is recommended that customer provided capital for future decommissioning (accumulated balance of depreciation of decommissioning assets and accretion expenses, less used amount) be included in the financing of rate base as no cost capital.

[71] Accumulated balance of depreciation of decommissioning assets and accretion expenses, less used amount by the end of the 2019/20 test year.
[72] InterGroup Consultants Report, P. 3-78

Future Applications

The Panel agrees with its consultant's recommendation that SaskEnergy provide more detailed explanations in future applications regarding intercompany allocations, productivity and efficiency measures, capital expenditures, and load forecast. These more detailed explanations include:

- Intercompany Allocations: If there are any material changes to the allocation percentages or the methodology, where relevant, SaskEnergy should review these details and rationale for the proposed change as well as any other alternatives that were considered.

- Productivity and Efficiency Measures: SaskEnergy provide a statement in the descriptions for each productivity and efficiency program that indicates how it meets the definition for productivity and efficiency initiatives. Restraint programs that have been, or that will be undertaken, should be clearly identified and described.

- Capital Expenditures: SaskEnergy provide more detailed updates regarding its capital plans and prioritization systems, particularly where significant new spending requirements are incurred (e.g. Information Systems).

- Load Forecast: Once Advanced Metering Infrastructure (AMI) is fully implemented and sufficient data becomes available, SaskEnergy review the reasonableness of its load forecast based on available monthly data.

Billing in Energy

The Panel has requested that SaskEnergy consider billing in energy in previous reports in order to reconcile the heating value variations in gas with the amounts billed to customers. Evidence indicates that some Saskatchewan residents benefit from higher-than-average heating values while others experience lower-than-average heating values. This means that some customers pay more than others to achieve the same heating energy because of their location in the province.

Average Consumption & Average Bill Impacts for 12 Month Period (2017/18)[73]

		Heat Value				Average 2017/18 Residential Average Bills					
	Estimated Average Number of Customers	Weighted Average HV (MJ/m^3)	Minimum Heat Value	Maximum Heat Value	Heat Value Variance	Annual Basic Monthly Charge ($)	Annual Delivery Charge ($)	Annual Commodity Charge ($)	Total Bill ($)	Total Bill Variance ($)	Total Bill Variance (%)
Regina	132,064	38.74	39.71	38.41	0.34%	273	262	397	932	- 2.00	-0.21%
Moose Jaw	**22,253**	**37.47**	**38.43**	**37.55**	**-3.04%**	**273**	**269**	**408**	**950**	**16.00**	**1.68%**
Weyburn	8,243	39.18	40.45	38.92	1.45%	273	259	393	925	- 9.00	-0.97%
Estevan	**8,356**	**42.29**	**43.52**	**41.79**	**8.70%**	**273**	**240**	**364**	**877**	**- 57.00**	**-6.50%**
Swift Current	13,489	37.81	38.20	37.58	-2.12%	273	268	407	948	14.00	1.48%
Yorkton	12,377	41.64	43.34	40.57	7.28%	273	243	370	886	- 48.00	-5.42%
Melville	4,098	39.18	42.72	38.13	1.45%	273	259	393	925	- 9.00	-0.97%
Saskatoon	152,673	38.10	38.42	37.93	-1.34%	273	266	404	943	9.00	0.95%
Prince Albert	25,865	38.90	39.10	38.50	0.75%	273	261	396	929	- 5.00	-0.54%
North Battleford	11,498	38.65	39.13	37.76	0.10%	273	262	398	934	-	0.00%
System Average	**390,915**	**38.61**	**39.38**	**38.15**	**0.00%**	**273**	**262**	**399**	**934**		

This table indicates the impact that heat value has in various locations in the province and the Panel has noted that this has resulted in ongoing fairness concerns for ratepayers and other stakeholders. Billing in energy would eliminate the need for forecasting heat value and the associated risks related to heat value variation in customer bills.

Heat value variances from forecast also impacts commodity revenues. For example, when heat value increases, customers require smaller volumes to achieve the same heating value, decreasing commodity revenues (which are based on volume). The GCVA mitigates SaskEnergy's financial risks related to heat value variances that impact commodity revenues. Commodity revenue variances from forecast are captured in the GCVA and collected (or refunded) in future periods. However, if amounts owed by ratepayers accrue in the GCVA it may compound the amounts owing from ratepayers (and required commodity rate increases) in future periods.

The actual impact that heat value variance has had on SaskEnergy commodity and delivery revenues is summarized in the table below, including the forecast impact for the 2018-19 fiscal year (assuming a commodity rate of 38.50 m^3/MJ). It should be noted that since 2015-16 the impact has been a reduction in commodity revenues of $14.956 million and the mid-application update has forecast another $1 million reduction for 2019-20 test year. This decrease in commodity revenue underscores the importance of resolving this issue as soon as possible.

Heat Value Revenue Impacts ($ millions)[74]

	2015/16	2016/17	2017/18	2018/19 (Forecast)
Impact to Delivery Revenue ($ millions)	$(5.531)	$(2.067)	$(2.450)	$(0.333)
Impact to Commodity Revenue (GCVA) ($ millions)	$(5.703)	$(3.188)	$(6.065)	$(1.097)

SaskEnergy notes that heat value impacts for 2018-19 and 2019-20 will depend on the difference between forecasted heat value and actual heat value. Generally, an actual heat value higher than forecast will result in lower actual delivery and commodity revenues. A lower heat value than forecast will result in actual higher delivery and commodity revenues.

[73] 1st Round Information Request 26(a).
[74] 1st Round Information Request 26 (c).

The impacts of billing in volume versus billing in energy have been mitigated in recent years due to several factors, such as the operation of the straddle plant in southeast Saskatchewan. However, it is uncertain if these factors will continue to reduce heat value variation in the future.

Although SaskEnergy has indicated a willingness to review measures required to transition to billing in energy, little progress has been made since the Panel initially raised its concerns in 2012. SaskEnergy has indicated that the reasons for deferring the transition have included the "current economic environment and fiscal restraints", and requirements for "conditions conducive to adding additional financial and staffing resources as well as the support of SaskEnergy's owner".[75]

In the 2018 application, SaskEnergy stated that it "continues to evaluate transitioning to billing in energy", "is in the process of a major technical upgrade to its customer information system" expected to be completed in 2019, and "upon completion a project to evaluate and transition to billing in energy will be initiated."[76]

The Panel recommends that SaskEnergy pursue measures required to shift to billing in energy as soon as possible.

[75] 2017 Delivery Service Rate Application, 1st Round Information Request 27 (c)
[76] Tab 24, Page 2

Analysis and Discussion on the Commodity Rate

Interim Commodity Rate

SaskEnergy proposed a two-part commodity rate proposal in which the rate would decrease effective November 1, 2018 followed by an additional final commodity rate decrease effective April 1, 2019. The rationale for this approach was that "SaskEnergy was seeking a commodity rate decrease that would provide customers a decrease large enough to be impactful during winter months, while at the same time leaving enough of a decrease for April 1, 2019 to offset the delivery service rate increase, while also allowing the Panel room to adjudicate the commodity rate."[77] This approach would "allow customers to benefit from a lower commodity rate during the winter period, when customers use the most natural gas, while allowing the panel adequate time to review the commodity information."[78]

The Panel approved the interim commodity rate reduction on October 19, 2018 on the provision that this was not a final review. Upon further consideration, the Panel now confirms this reduction and agrees with the requirement for, and time of, the effective date for the commodity rate reduction of November 1, 2018. This approach also recognizes that the interim and final rates provided a measure of rate stability for customers since they would not be faced with a material bill reduction followed by a bill increase related to the delivery rate increase within a four month period.

The rate adjustment recommended on November 1, 2018 was an interim rate adjustment to allow for a more thorough examination of assumptions and data used to generate a final rate recommendation. After a final review, the Panel recommends to the Minister that the Panel's approval for the interim commodity rate decrease effective November 1, 2018 of 13.87 cents/m^3 ($3.65/GJ) to 11.36 cents/$m^3$ ($2.95/GJ) be confirmed.

Final Commodity Rate

SaskEnergy proposed a commodity rate effective April 1, 2019 that does not fully clear the balance in the GCVA at the end of the test year and would maintain a $3.3 million balance in the account at the end of the test period on March 31, 2020. SaskEnergy stated that it was "deviating from normal practice due to the current low price environment, and the increased probability of natural gas prices rising compared to declining further," and "leaving a modest balance in the GCVA is expected to help mitigate a higher commodity rate in the future." The corporation also noted that "if there is opportunity for a commodity rate decrease to offset a delivery rate increase, this strategy will be used in order to provide customers with overall bill stability."[79]

The Panel's consultant does not support this approach because the purpose of the GVCA is to provide SaskEnergy the opportunity to recover the cost of gas sold to customers without any mark-up. Rates are traditionally designed to target a GCVA balance of zero to minimize the impact of intergenerational equity and fairness. Using the GCVA balance as a tool to mitigate potential future commodity or delivery rate impacts would appear to alter the core purpose and function of the account. The proposed approach does not have any prior precedent and would be a significant change in how the account has historically operated. Although SaskEnergy has indicated that this is a one-time request with future commodity rate applications expected to target a zero GCVA balance,[80] setting rates that deviate from normal regulatory practice and past precedents would appear to be unwarranted unless under exceptional circumstances.

The Panel notes that SaskEnergy reviews the commodity rate each spring and fall, and as a matter of course, expects to adjust its commodity rate once or twice a year. The corporation has also been able to maintain the same

[77] 1st Round Information Request 1 (a) (Commodity)
[78] Ibid
[79] 1st Round Information Request 1 (d) and (e) (Commodity)
[80] 1st Round Information Request 1 (e) (Commodity)

commodity rate for the past two years without the GCVA growing beyond $20 million (either owing to or from customers). As well, SaskEnergy has fixed the price on a large portion of its forecasted natural gas purchase for the next five years. If prices remain near current levels, fewer commodity rate changes are anticipated over this period.

The proposed commodity rate in the original application was based on a heat value of 38.50 MJ/m^3, which resulted in a final commodity rate of 10.20 cents/m^3 ($2.65/GJ) effective April 1, 2019. SaskEnergy revised the heat value in the update to 38.75 MJ/m^3 which would result in a final commodity rate of 10.20 cents/m^3 or $2.63 GJ.

SaskEnergy has indicated that a commodity rate of $2.575/GJ effective April 1, 2019 would clear the GCVA balance at the end of the 2019-20 test period.[81] The Panel believes that clearing the balance in the GCVA maintains the original rationale behind the account and recommends the revised rate. After a final review of the commodity rate, the Panel recommends to the Minister that the proposed commodity rate effective April 1, 2019 that would see a further decrease to $2.63/GJ be revised to $2.575/GJ to eliminate any outstanding balance in the GVCA.

[81] Revised Response to 2nd Round Information Request 4 (a) (Commodity)

Risks and Considerations

The following should not be considered a complete analysis of all the risks that SaskEnergy is subject, but have been considered by the Panel as potential risks and considerations in making these recommendations. These risks may appear at a future date and have an impact on the customer, the utility and the public. All stakeholders should be aware of these risks and considerations as they may have an impact on future rate applications.

Natural Gas Prices

Although natural gas prices have remained low for some time, it is expected that over time, natural gas prices will increase and this may drive future commodity rate increases. Price fluctuations are due to the dynamics of supply and demand and can have an impact on future applications. Variances are tracked in SaskEnergy's GCVA as they occur and pass through to the ratepayer.

Weather

Weather remains a constant risk for SaskEnergy. If weather is colder than normal, then its revenue will be higher and customer bills will increase since more volume will be consumed. If weather is warmer than normal, customers will consume less natural gas, resulting in lower bills and lower delivery revenue for SaskEnergy.

Carbon Tax

The federal carbon tax is set to begin on April 1, 2019 at $20/tonne, increase to $30/tonne on January 1, 2020, and then increase annually by $10/tonne to $50/tonne by 2023. SaskEnergy estimates that the $20/tonne carbon tax will result in a charge of $0.0391/$m^3$ for natural gas.[82] This would result in an estimated $9.10 increase in monthly residential bills or an annual increase of $109 for 2019.[83]

The Saskatchewan government has asked the Provincial Court of Appeal to rule on whether the federal carbon tax plan is constitutional, however, SaskEnergy is preparing to collect a carbon tax should a carbon tax be required to be collected starting April 1, 2019.[84]

Interest Rates

SaskEnergy holds both short term and long term debt. With the significant capital plan of SaskEnergy, financing costs associated with this plan could be impacted going forward which could put additional upward pressure on delivery rates. However, interest expense is a forecast risk that is taken by SaskEnergy and any losses or benefits that accrue due to higher or lower actual interest expense compared to forecast are borne or attributable to the corporation.

Collective Agreements

The collective agreement between SaskEnergy and its employees' union, Unifor, expired on January 31, 2017. There is risk that the overall collective agreement rates may be higher than SaskEnergy is forecasting, which may apply pressure to rates.

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[82] 1st Round Information Request 21 (d), 2018 Commodity and Delivery Service Rate Application

[83] Prepared based on 1st Round Information Request 21 (d), 2nd Round Information Request 18 (b), 2018 Commodity and Delivery Service Rate Application.

[84] 1st Round Information Request 21 (d), 2018 Commodity and Delivery Service Rate Application

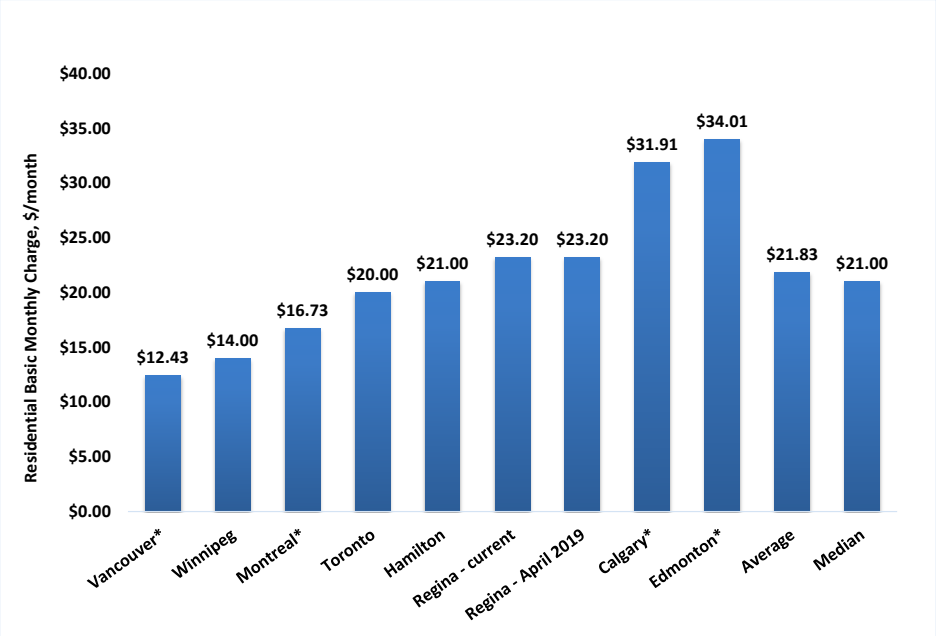
The Competitiveness of the Proposed Rates

If the proposed rate changes were implemented, SaskEnergy's delivery service rates would remain lower than average for major Canadian centres for all customer classes, and the commodity portion of the bills would be in the mid-point range. Based on this information, the Panel has concluded that SaskEnergy's rates will remain competitive with other jurisdictions if the requested rates are implemented.

The following is a detailed analysis per customer class. The Panel did not request an assessment of competitiveness for small industrial customers from the consultant since these customers tend to have unique operating requirements that make comparisons across jurisdictions difficult.

Residential Rates

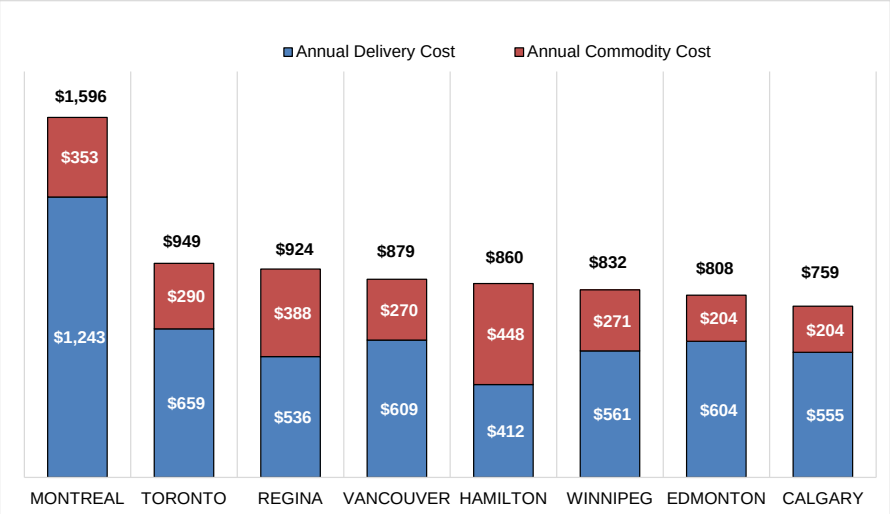
Residential Basic Monthly Charge Comparison ($/Month)[85]



This figure compares the basic monthly charges for all residential customers and the results indicate that the basic monthly charge is higher compared to the five major Canadian centres, but lower compared to Edmonton and Calgary.

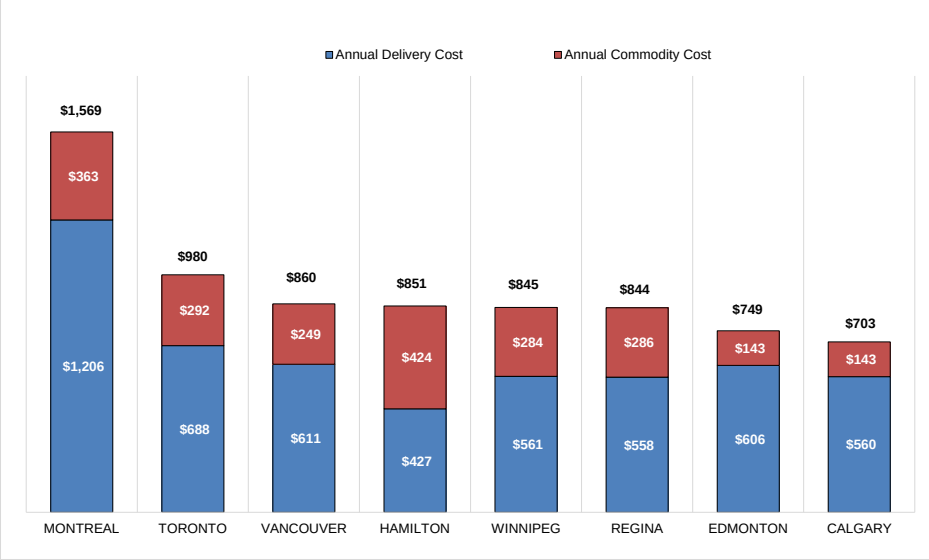
[85] Regina proposed rate from Schedule 5 of 2018 Commodity and Delivery Service Rate Application. Vancouver charge from FortisBC, as of January 1, 2019: http://www.fortisbc.com/NaturalGas/Homes/Rates/Mainland/Pages/default.aspx, fixed charges for Calgary and Edmonton are from ATCO Gas for South and North, as of December 1, 2018: http://www.atcogas.com/Rates/Current_Rates/ plus a Direct Energy Regulated customer charge, current rates available at: https://www.directenergyregulatedservices.com/images/docs/181126-DERS-Dec-2018-Interim-South-DRT-Rate-Schedules.pdf and https://www.directenergyregulatedservices.com/images/docs/181126-DERS-Dec-2018-Interim-North-DRT-Rate-Schedules.pdf, Winnipeg charge from Centra Gas, current rates as of November 1, 2018: https://www.hydro.mb.ca/regulatory_affairs/energy_rates/natural_gas/current_rates.shtml, Toronto charge from Enbridge gas, current rate as of April 1, 2018: https://www.enbridgegas.com/Understanding-gas-rates, Hamilton charge from Union Gas, Southwestern Ontario, rates as of October 1, 2018: https://www.uniongas.com/residential/rates/current-rates/rate-m1, Montreal rate from Energir, rate as of December 1, 2018: https://www.energir.com/~/media/Files/Affaires/Tarif/conditionsservicetarif_an.pdf?la=en [all web sites are accessed on December 10, 2018].

Annual Average Residential Delivery and Commodity Costs October 2017 – September 2018
(based on average consumption of 2,800 m3/year)[86]



This figure shows the actual annual residential delivery and commodity costs for October 2017 through September 2018. Of the jurisdictions surveyed, SaskEnergy had the third highest bills for residential customers at the assumed average consumption level and based on October 2017 to September 2018 rates.

Annual Average Residential Delivery and Commodity Costs based on Most Recent Rates
(based on average consumption of 2,800 m^3/year)[87]

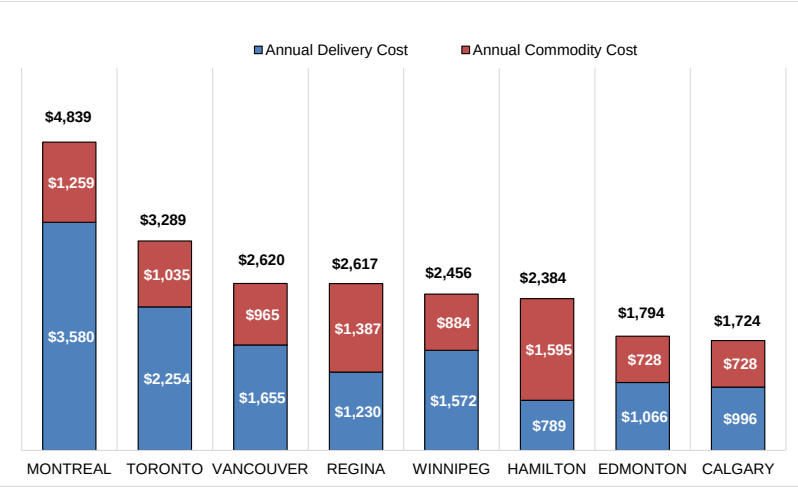


This figure compares bills at most recent rates, including rates proposed by SaskEnergy effective April 1, 2019, which shows that SaskEnergy would have the third lowest bills with proposed April 1, 2019 rates due to reduced commodity rates.

[86] Tab 22, page 7. 2018 Commodity and Delivery Service Rate Application.
[87] 1st Round Information Request 22 (b), 2018 Commodity and Delivery Service Rate Application. SaskEnergy notes that the figure reflects proposed SaskEnergy rate effective April 1, 2019; all other jurisdictions are based on the latest available information and are as of October 2018 with the exception of Edmonton and Calgary [ATCO Gas proposed delivery rates effective January 1, 2019 and Rider Z effective Feb 1, 2019 for Edmonton/Calgary].

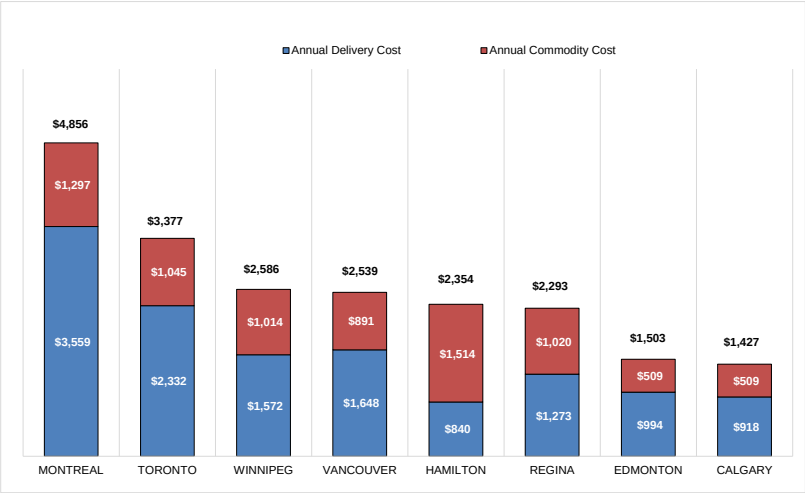
Commercial Small Rates

Commercial Small Delivery and Commodity Costs October 2017 – September 2018 (based on consumption of 10,000 m3/year)[88]



This figure provides a comparison of average annual bills for commercial small customers for rates from October 2017 to September 2018.

Commercial Small Delivery and Commodity Costs for Most Current Rates (based on consumption of 10,000 m3/year)[89]



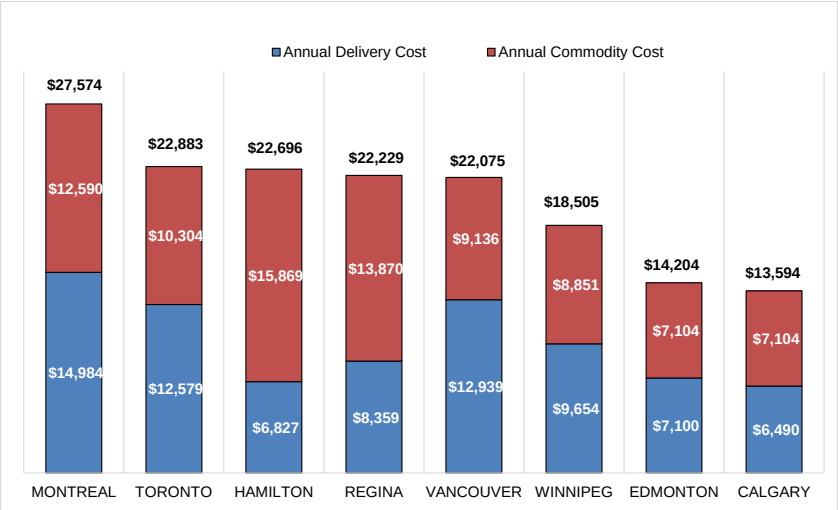
This figure provides a comparison of commercial small bills for the most current rates which includes proposed bills for SaskEnergy. This shows that commercial small bills in Regina are expected to be the third lowest of the eight jurisdictions surveyed under the proposed rates due to reduction in commodity rates.

[88] Tab 22, page 7. 2018 Commodity and Delivery Service Rate Application.

[89] 1st Round Information Request 22 (b), 2018 Commodity and Delivery Service Rate Application. SaskEnergy notes that the figure reflects proposed SaskEnergy rate effective April 1, 2019; all other jurisdictions are based on the latest available information and are as of October 2018 with the exception of Edmonton and Calgary [ATCO Gas proposed delivery rates effective January 1, 2019 and Rider Z effective Feb 1, 2019 for Edmonton/Calgary].

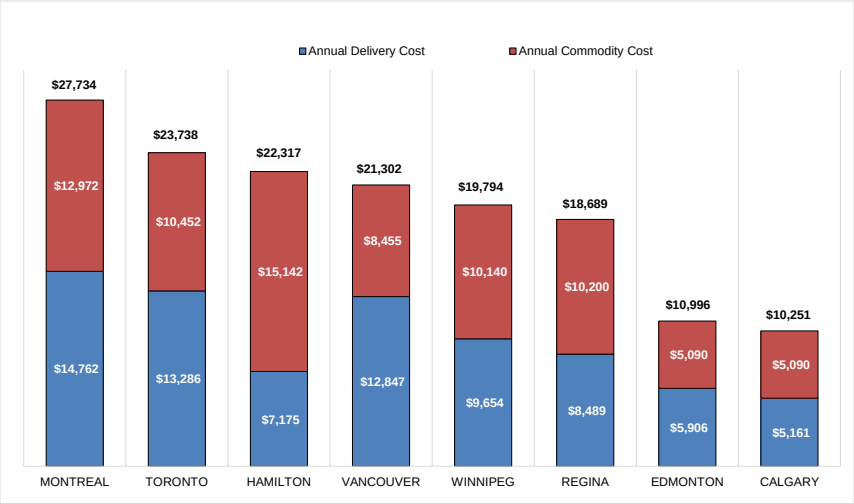
Commercial Large Rates

Commercial Large Delivery and Commodity Costs for October 2017 – September 2018 (based on consumption of 100,000 m3/year)[90]



This figure provides a comparison of average annual bills for commercial large customers for rates from October 2017 to September 2018.

Commercial Large Delivery and Commodity Costs for Most Current Rates (based on consumption of 100,000 m^3/year)[91]



This figure provides a comparison of commercial large bills for the most current rates and includes proposed bills for SaskEnergy. The results show that commercial large bills in Regina are expected to be the third lowest of the eight jurisdictions surveyed under the proposed rates due to the reduction in commodity rates.

[90] Tab 22, page 7. 2018 Commodity and Delivery Service Rate Application.
[91] 1st Round Information Request 22 (b), 2018 Commodity and Delivery Service Rate Application. SaskEnergy notes that the figure reflects proposed SaskEnergy rate effective April 1, 2019; all other jurisdictions are based on the latest available information and are as of October 2018 with the exception of Edmonton and Calgary [ATCO Gas proposed delivery rates effective January 1, 2019 and Rider Z effective Feb 1, 2019 for Edmonton/Calgary].

The Impacts of the Proposed Rates

Impact on the Customer

Customer bills include variable or volumetric rates (commodity rate and delivery rate) and a fixed charge (basic monthly charge). Bill impacts will vary depending on customer class and usage levels.

Customer Bill Impacts from Proposed Rate Changes[92]

	Commodity Rate Decrease		Delivery Service Rate Increase		Total Bill Impact	
	$/Month	Annual Bill % Change	$/Month	Annual Bill % Change	$/Month	Annual Bill % Change
Residential	-$8.50	-11.1%	$1.76	2.3%	-$6.74	-8.8%
Commercial Small	-$39.99	-14.6%	$4.47	1.6%	-$35.52	-13.0%
Commercial Large	-$520.0	-17.0%	$16.0	0.5%	-$504.75	-16.5%
Small Industrial	-$2,435.0	-20.2%	$13.0	0.1%	-$2,422.00	-20.1%
Average		-12.7%		1.9%		-10.8%

The above table summarizes the bill impacts for average customers in each customer class. At average consumption levels, customers in all rate classes are expected to experience overall bill decreases due to the reduced commodity rates.

Although customers may expect to see bill decreases, these decreases could be impacted by the federal carbon tax, which is expected to be implemented on April 1, 2019. The tax starts at $20/tonne this year and will increase to $30/tonne by January 1, 2020. The tax will continue to increase by $10/tonne annually to $50/tonne by 2023. SaskEnergy estimates that with a $20/tonne carbon tax, customers will see a charge of $0.0391/m3 for natural gas. Residential customers would see a 13% bill increase in 2019 with a $20/tonne carbon tax; commercial small customers will see an 18% increase, and commercial large customers will see a 22% bill increase (see table below).

Bill Impact from Carbon Tax for Average Usage by Customer Class[93]

Monthly Bill Impact

	Average Annual Consumption, m^3	Monthly Bill at Proposed Rates $/Month	2019 with $20/tonne		2020 with $30/tonne		2023 with $50/tonne	
			$/Month	Monthly Bill % Change	$/Month	Monthly Bill % Change	$/Month	Monthly Bill % Change
Residential	2,779	$70.0	$9.1	13.0%	$13.6	19.4%	$22.8	32.5%
Commercial Small	13,074	$238.0	$42.6	17.9%	$63.9	26.9%	$106.7	44.8%
Commercial Large	170,147	$2,553.5	$554.4	21.7%	$832.3	32.6%	$1,388.1	54.4%

Annual Bill Impact

	Average Annual Consumption, m^3	Annual Bill at Proposed Rates $/Year	2019 with $20/tonne		2020 with $30/tonne		2023 with $50/tonne	
			$/Year	Annual Bill % Change	$/Year	Annual Bill % Change	$/Year	Annual Bill % Change
Residential	2,779	$840.0	$109.0	13.0%	$163.0	19.4%	$273.0	32.5%
Commercial Small	13,074	$2,856.0	$511.0	17.9%	$767.0	26.9%	$1,280.0	44.8%
Commercial Large	170,147	$30,642.0	$6,653.0	21.7%	$9,988.0	32.6%	$16,657.0	54.4%

[92] Page 1, 2018 Commodity and Delivery Service Rate Application.
[93] Prepared based on 1st Round Information Request 21 (d), 2nd Round Information Request 18 (b), 2018 Commodity and Delivery Service Rate Application.

Impact on the Crown Corporation – SaskEnergy

The Panel recognizes that SaskEnergy requires a rate increase to continue to meet its ongoing investments regarding safety, system integrity and major growth infrastructure, as well as meeting its return on equity requirements. Upon review and analysis, the Panel is confident that taking into consideration the foregoing recommended adjustments to the revenue requirement forecast that SaskEnergy can meet these commitments and ROE target of 8.14% with an approved 3.4% rate increase.

The delivery service revenue at the proposed rates (3.4% increase) is forecasted to generate $278.671 million providing incremental revenue of $9.3 million.

Panel's recommended adjustments to the 2019-20 Revenue Requirement and Net Income forecast

Impact to the 2019/20 Revenue Requirement and Net Income

	Mid-Application Update	Estimated Adjustment for NEB Decision on TransCanada PipeLines Limited	After Adjustment	Required Changes as per Review	*Change*	*Change %*
	A	B	C=A+B	D	*E=D-A*	
Operating & Maintenance Expense[1]	136,457	0	136,457	135,977	(480)	-0.4%
Transportation and Storage Expense[2]	54,697	(680)	54,017	55,724	1,027	1.9%
Depreciation Expense	48,405	0	48,405	48,405	0	0.0%
Tax Expense	7,270	0	7,270	7,270	0	0.0%
Interest Expense[3]	30,638	0	30,638	29,621	(1,017)	-3.3%
Revenue Requirement Before Net Earnings	**277,467**	**(680)**	**276,787**	**276,997**	**(470)**	**-0.2%**
Other Revenue	(30,411)	0	(30,411)	(30,411)	0	0.0%
Net Revenue Requirement Before Net Earnings	**247,056**	**(680)**	**246,376**	**246,586**	**(470)**	**-0.2%**
Delivery Service Revenues at Proposed Rates[4]	279,204		279,204	278,671	(533)	-0.2%
Net Earnings[5]	**32,148**		**32,828**	**32,085**	**(63)**	**-0.2%**
Equity Portion of Rate Base[6]	395,056		395,056	394,279	(777)	-0.2%
Return on Equity	8.14%		8.31%	8.14%	0.00%	
Net Earnings to get 8.30% ROE	32,790		32,790	32,725		
Revenue Deficiency to get 8.30% ROE	(642)		38	(640)		

Notes:

[1] Vacancy rate calculation adjustment [section 3.1.1]
[2] Underestimation of transportation expense [section 3.2]
[3] Reflect net customer funding for future decommissioning included as no cost capital reducing debt and portion of Distribution Toll lag days adjustment from 82.9 to 45.6
[4] Assumes no change in proposed rates
[5] Column A and C based on 8.14% ROE and rates proposed by SaskEnergy and Column D on 8.14% ROE and the 3.4% rate recommended by the Panel
[6] Distribution Toll lag days from 82.9 to 45.6 plus Reflect net customer funding for future decommissioning included as no cost capital

As noted in the section "Operations and Maintenance (O & M)", the Panel discussed and recommended a $0.480 million reduction in labour cost relative to vacancy management. Additionally, as noted in the "Transportation and Storage" section, there were two issues identified during the discovery and subsequent processes. The underestimation of volumes delivered added $ 1.707 million to the transportation forecasted expense and subsequently SaskEnergy also noted that as a result of the NEB decision on mainline tolls will reduce the LDC transportation expenses by $0.680 million. Coupled together, transportation and storage expense forecast increased $1.027 million which is now forecasted to be $ 55.724 million up from the $54.697 in the mid-application update.

The final adjustments to the revenue requirement by the Panel are in the section headed “Rate Base and Capital Structure” recommended two adjustments, one to reflect the reduction in working capital (revenue requirement reduction of $0.060 million) and lastly to reflect net customer funding for future decommissioning included as no cost of capital ($0.956 million) for a total of $ 1.017 million reduction.

SaskEnergy has identified $4.4 million in estimated corporate savings in 2017-18 related to productivity and efficiency measures. For the 2018-19 fiscal year, SaskEnergy targeted a further $4 million in annual efficiency savings. The Panel believes it is vital for the corporation to continue these initiatives and provide savings to ratepayers in future periods.

There are other recommendations in the report that will have an impact on the manner in which SaskEnergy provides information to the Panel. These recommendations are designed to make future applications more efficient and reduce the amount of time spent on obtaining the necessary data.

Impact on the Public

Since SaskEnergy is a Crown-owned utility, all citizens of Saskatchewan have a vested interest in the corporation’s operations. A utility that provides safe and reliable natural gas service throughout the province is essential to the economic development and well-being of the province. The recommended rates will enable SaskEnergy to achieve an industry comparable ROE 8.14%.However, the public should be aware that there will continue to be upward pressure on rates due to SaskEnergy’s continued capital spending program.

Role of the Saskatchewan Rate Review Panel

Authority

Through Order-in-Council dated December 22, 2018, the Minister of Crown Investments Corporation (the Minister) appointed a Ministerial Advisory Committee known as the Saskatchewan Rate Review Panel (the Panel), with the mandate that it shall:

> *… conduct a review and provide an opinion of the fairness and reasonableness of proposed Crown corporation rate changes, referred to the Panel by the Minister of Crown Investments Corporation; and incorporate as part of its mandate specific terms of reference for particular Crown corporation rate change reviews that may be attached by further Minister's Order.*

Whether in the original Order-in-Council establishing the Panel (437/2000 dated July 27, 2000), or in the Terms of Reference for particular reviews, the Panel has always been instructed to consider: "*…the interests of the customer, the Crown corporation, and the public*."

The mandate of the Panel extends to three Crown corporations in Saskatchewan – SaskEnergy, SaskPower and SGI's Saskatchewan Auto Fund. Serving as an advisory body to the Minister Responsible for Crown Investments Corporation, the Panel provides independent advice on rate proposals from the above-noted corporations. The final decision about these proposals continues to rest with the Saskatchewan government.

Members of the Panel

The following members have been appointed to serve on the Saskatchewan Rate Review Panel:

Chair	Albert Johnston, Saskatoon
Vice-Chair	Delaine Barber, Weyburn
Members	Burl Adams*, Kelvington; Glenn Dutchak, Canora; Kim Hartl, Lake Lenore; Daryl Hasein, Biggar; Duane Hayunga, Prince Albert; Steve Kemp, Regina; and Lyle Walsh*, Yorkton.

*denotes terms which ended December 31, 2018

Panel's Terms of Reference

The Minister issued an Order on September 26, 2018 establishing the Terms of Reference guiding the Panel's review of SaskEnergy's Rate Application. The Minister's Order and the Terms of Reference for this application identified several factors that the Panel is to consider in conducting its review, as well as various parameters that are outside the Panel's purview. For the delivery rate review, these parameters include:

- The rate structure (i.e. components and classifications)
- The budgeted capital allocation, the base rate, and established corporate policies
- The long-term target rate of return on equity of 8.30%, as approved in the 2018-19 business plan, using industry based rate setting methodology and excluding customer contributions for the distribution utility,
- The existing service levels
- The revenue-to-cost ratio target range of 0.95 to 1.05
- All transportation and storage rates including those set by TransGas Limited.

The Minister's Order for this review called for the Panel to complete its work no later than February 4, 2019.

Review Process for the Application

Consultant

InterGroup Consultants Ltd. (the consultant) was engaged by the Panel as an independent technical adviser to review the fairness and reasonableness of SaskEnergy's proposed rate change, and to provide an independent report including recommendations that would be consistent with the Terms of Reference for the Panel's review of the application. The consulting team was led by Mona Pollitt-Smith, a principal at InterGroup Consultants Ltd.
At the direction of the Panel, the consultant conducted a detailed analysis of the application, asked two rounds of information requests and supplementary questions (all posted on the Panel's website), and had individual discussions with SaskEnergy staff to clarify specific points. The consultant reviewed public comments to the Panel, and participated in several meetings and conference calls with the Panel during the review process before presenting its final report to the Panel on January 15, 2019.

Public Consultations

In reviewing SaskEnergy's application, the Panel invited public comment. The public consultation process included:

- Submissions received by mail;
- Online messages received through the Panel's website;
- Messages received directly through the Panel's email address;
- Messages received through the Panel's toll-free voice mailbox; and
- Messages posted to the Panel's Facebook and Twitter accounts.

A public meeting was held in Regina on October 17, 2018. Members of the public were also invited to view the meeting online and type their questions from their computer, tablet or smartphone during the live broadcast.

All methods for public input were advertised in the two major daily newspapers, and information was disseminated through Facebook and Twitter. SaskEnergy's application received news coverage immediately after it was announced. Copies of the application were available to the public at its offices and on the Panel's website.

There were a limited number of public comments on this application; however, the comments that were provided were critical of the Delivery Service Rate increase and supportive of the commodity rate decrease. Concerns were expressed that it is becoming increasingly difficult for low income earners and those on fixed incomes to pay higher rates. Here is a sampling of the comments:

How are people on limited income going to be able to afford higher rates? I am on equal payments now but I know people who aren't and an increase will hurt them.

Decrease the Commodity Rate and no increase to the Delivery Charge. Tell SaskEnergy to find efficiencies.

We already pay enough. A lot of us have a hard time paying our bills now, let alone if it goes higher.

Seniors can't afford the high cost of heating our homes.

A small portion of each bill should go into an infrastructure fund for future required upgrades to the system.

All submissions and a transcript of the public meeting are available on the Panel's website at www.saskratereview.ca.

In Appreciation

The Panel thanks SaskEnergy for the timely and helpful assistance it provided throughout this application.

The Panel thanks InterGroup Consultants Ltd. for its thorough analysis of the application.

The Panel thanks Gerry Forrest, our general consultant, for his ongoing assistance in the work of the Panel.

The Panel thanks technical writer Pat Rediger for his assistance in preparing this report.

Finally, the Panel wishes to acknowledge the members of the public who participated in the review process. All contributions were received and evaluated by the Panel during its decision-making process.

For More Information

For more information on this review, please visit the Saskatchewan Rate Review's website at www.saskratereview.ca. The site contains SaskEnergy's 2018 Rate Application, SaskEnergy's public presentation on the application, the Panel's terms of reference, information requests to SaskEnergy and the responses, video of the public meeting, public submissions and comments, the technical consultant's report, and the Panel's media releases.