May 15, 2009

Via E-Mail and Courier

Kirsten Walli
Board Secretary
Ontario Energy Board
PO Box 2319
2300 Yonge Street
Suite 2700
Toronto, ON
M4P 1E4

Re: Commodity Pricing, Load Balancing and Cost Allocation Methodologies for Natural Gas Distributors EB-2008-0106

Dear Ms. Walli,

Please find attached the Gas Marketer Group's (Direct Energy Marketing Limited, Ontario Energy Savings L.P., and Superior Energy Management Gas L.P.) Final Argument in the above noted proceeding.

Should you have any questions or concerns, please contact the undersigned.

Yours faithfully

Original Signed by

Ric Forster
Director
Government & Regulatory Affairs

Cc: Mr. Norm Ryckman, Enbridge Gas Distribution
Mr. Chris Ripley, Union Gas Limited
Mr. Mark Bristoll, Natural Resources Gas Limited

2225 Sheppard Avenue East, Atria III, Suite 500, Toronto, ON, M2J 5C2 Tel: 416-718-5942 Fax: 416-758-4272
ric.forster@directenergy.com

GAS MARKETER GROUP (GMG) (DIRECT ENERGY MARKETING LIMITED,
ONTARIO ENERGY SAVINGS L.P., and
SUPERIOR ENERGY MANAGEMENT GAS L.P.)

Final Argument re: Commodity Pricing, Load Balancing, and Cost Allocation Methodologies for Natural Gas Distributors

Introduction

1. The following is the final argument of the Gas Marketer Group ("GMG") comprised of Direct Energy Marketing Limited, Ontario Energy Savings L.P., and Superior Energy Management Gas L.P.

2. The GMG companies have affiliates in many jurisdictions across North America and have attempted to draw upon this multi-jurisdictional experience to offer best practices in utility rate setting for consideration by the OEB, while recognizing that there are considerations particular to the Ontario marketplace.

3. In the Natural Gas Forum Report ("NGF"), the Ontario Energy Board (the "Board") determined there was a need to balance the provision of an accurate price signal for customers with price stability when determining the appropriate rate adjustment mechanism for utilities. The Board recognized the need to evaluate the rate setting mechanisms employed by the utilities, and as such, created this generic proceeding to investigate such matters.

4. The GMG believes that much has been offered by all parties for consideration in this proceeding, and that the evidentiary process in generic proceedings should allow for the further development of the market in a way that will be beneficial for customers and market participants. Furthermore the GMG believes the evidence supports the conclusion that it is possible to make improvements in the current rate setting methodologies in order to increase the transparency and accuracy of rate adjustments, while also lessening the likelihood of large dispositions and providing price stability.

5. The GMG is very grateful for the opportunity to present its views to the Board and appreciates being a part of this consultative process. The natural gas market in Ontario is a complex competitive market and the involvement of a broad array of stakeholders in this proceeding demonstrates the Board's commitment to improving this competitive market for the benefit of customers and all stakeholders.

Review of Quarterly Rate Adjustment Mechanism for Natural Gas Distributors

Trigger Mechanism

6. The GMG accepts the proposal as put forth by Enbridge and Union that there be no trigger mechanism.

Price Adjustment Frequency and Forecast Period

7. The GMG believes that the current rate setting methodology employed by the utilities is not appropriate as it has resulted in large PGVA balances and rate riders over the last number of years. An example of this can be found in Table 2 of the GMG's evidence (Exhibits E8, E14, E19, page 8) which demonstrates that Enbridge has over-collected from its customers in 11 of the 12 quarters from January 2006 to December 2008, and was acknowledged by the Enbridge panel in cross-examination (2 Tr. 13, lines 2-21). This continual over-collection from customers is a direct result of the forecasting and rate

setting methodologies employed by the utilities, which clearly distorts pricing signals. The GMG submits that this distortion of price signals does not allow customers to make informed consumption and provider choices. Nor does it reflect proper cost causality, as the PGVA balances are currently distributed over changing customer bases from quarter to quarter due to customer migration, burner tip equipment changes, and consumption pattern changes; instead of being disbursed in a more timely fashion.

8. The ideal rate setting methodology in GMG's submission is one that involves monthly price-setting, monthly forecasting and monthly dispositions. Given the profound change in gas procurement practices by the major LDC's in Ontario since the last NGF, the GMG submits that an evolution toward monthly price setting is logical. Since the utilities are currently exposing customers to all monthly (or spot) index price exposure, the GMG submits that the price should be changed monthly to reflect the most accurate price. Monthly price setting would not only more closely match procurement practices, it would more closely match the cost/benefit of this default service to the customers actually receiving this service, hence reducing intergenerational mismatches.

9. Enbridge stated in its pre-filed evidence that "the 12 month forecast reflects the manner in which EGD incurs its gas supply costs" (pg 9 of 60 para 31 – EGD evidence). The GMG respectfully submits that while the 12 month forecast may be reflective of the volumetric profile purchased by EGD, it does not reflect the actual price incurred by EGD, since the utilities are exposing customers to actual short term monthly index costs. The GMG agrees with statements made by both EGD and Union that any forecast price would prove to be more accurate if the price forecast was calculated as close to the actual flow of gas as practicable, and furthermore that balances in the PGVA accounts are directly related to the accuracy of the forecast. (2 Tr. 34, lines 10-27 and 1 Tr. 31, line 21-32, line 10). The GMG supports reducing these timing differences where practicable.

10. The utilities in this proceeding have raised concerns that a monthly price setting mechanism based on a monthly forecast with a monthly disposition of PGVA balances (MRAM) is impractical, as Ontario relies on storage to meet its supply obligations. Furthermore the utilities believe that the implementation of an MRAM will lead to price volatility, increased costs, and increased regulatory burden.

11. The fact that Ontario relies on storage and long haul transportation should not preclude a change to monthly price setting. The infrastructure requirements to serve a gas market are quite separate from the mechanism used to establish supply prices for system customers. Costs for transportation and storage are incurred and cleared monthly in the wholesale gas market. As cited by the GMG during the proceeding, the real short term market price incurred by system customers can be reflected to system customers monthly, in a transparent fashion, as is done in both Alberta and Ohio (which both employ MRAM methodology).

12. Monthly price setting will be more reflective of the wholesale market which <u>is</u> the cause of any volatility in natural gas prices. Frequency in price setting does not necessarily translate into a more volatile price. The notion that QRAM dampens price volatility is not accepted by the GMG due to the fact that the Ontario utilities procure supply in the month ahead and spot markets. Customers will incur the wholesale price volatility whether it be through the stated commodity price or subsequent rate riders. The impact to the bottom line of the customer bill will be the same. The GMG believes that the more reflective the rates are of the market price of the gas commodity, the more responsive consumers will be in their actions regarding provider and consumption choice.

13. While the Manitoba Public Utilities Board ("PUB") dealt with a similar issue in 2007 and determined that monthly price setting was not the appropriate rate adjustment method for the province's natural gas utilities, it is important to note that this decision is not applicable to the situation in Ontario. Specifically the competitive market is much further developed in Ontario than in Manitoba. At the time of the PUB decision, for example, Manitoba's market remained dominated by the government-owned utility.

Ontario, on the other hand, has had an open and competitive market for over 20 years with multiple competitors. Due to the more advanced market in Ontario, the OEB is more progressive in its regulatory approach than the PUB or the British Columbia regulators who, in considering the frequency of the rate-setting mechanism, were faced with markets that were not yet developed nor nearly as competitive as in Ontario.

Calculation of Reference Price

14. Ideally, the GMG believes that the Ontario market should be fully unbundled, segregating the gas commodity and all ancillary services required to deliver the commodity to the consumer including storage and transportation (both long and short haul). However, the GMG recognizes that unbundling is not the subject matter of this proceeding. Nonetheless, a step in the right direction would be a single, mechanistic, transparent calculation of Reference Price based on the month ahead index at a designated trading point.

15. This approach is beneficial from a consumer perspective as a published index will clearly show consumers how their gas bills are being calculated and will allow them to make conservation decisions on a fully informed basis. This creates a truly transparent system.

16. Once the OEB determines the issue of reference price, the parties should design a system to provide a clear and transparent index-based reference price to be used in the calculation of the monthly commodity rate.

17. As discussed by the GMG panel in the Hearing, the Ohio retail gas market has evolved to a point where the major gas distribution companies have a default commodity supply price for system customers that is calculated by adding the appropriate transportation/storage/service differential to the NYMEX prompt month settlement price. This allows for all customers in that jurisdiction to receive short term price signals that are consistent with utility procurement protocols.

Deferral and Variance A/C Disposition

18. As mentioned earlier, the GMG believes that the current Ontario default commodity rate setting methodology is not appropriate as it has resulted in large PGVA balances and rate riders over the last number of years. In order to give the clearest picture, PGVA balances should be cleared as frequently as the rate setting period. However at the very least, PGVA balances must be cleared on the same frequency as the forecasting period. The matching of PGVA clearance and forecasting will provide a clearer linkage between how the utilities forecast their supply rates and how the utilities recover supply costs from customers, which minimizes intergenerational cross-subsidization.

Impact on Revenue Requirement

19. The GMG supports that changes in the utility revenue requirement should be reflective of changes in the Reference price.

Filing Requirements

20. The GMG believes that through this proceeding a consistent, transparent method for the facilitation of a monthly rate setting process can be established which can easily be understood by all parties. The GMG has provided the GCFR process in Alberta as an illustration of the mechanics used in establishing a price based on timely market data, and recognizes that this process should be modified to account for the impacts of storage, as illustrated in GMG/BOMA & LPMA IR#2(b).

21. As changes of this nature have an impact on customers, stakeholders, and the Board, the GMG supports Enbridge's approach in paragraph 88 of its pre-filed evidence to allow the Board and stakeholders to determine the calculation and process for rate adjustment applications. The GMG believes that if all parties have input into the information used and the calculation of rates that this will allow for an expedited regulatory approvals process. Such a process could allow for the expeditious implementation of rates, without negating the ability of parties to challenge aspects of a particular MRAM filing, once rates are implemented. As noted in Union's response to GMG IR #12(f) (Exhibit IR8.12), Union agrees that the primary drivers for using the current lead time for setting rates are directly related to the timing of the regulatory approvals and notice periods in the current QRAM process. Furthermore, in the same response, Union indicated that gas price forecasts made closer to the effective supply date would tend to be more accurate.

Load Balancing

22. With respect to Union, the GMG submits that its current practices are acceptable and Union should maintain status quo. The GMG fully supports Enbridge's proposal to adopt a weather normalized MDV re-establishment as a positive step that should be supported by the Board. Furthermore, the implementation of such capabilities should be implemented as soon as possible to address customer mobility and delivery issues as a result of recent GDAR changes.

23. In order to provide an ideal degree of flexibility in the market, weather normalized MDV re-establishment and multi-point balancing should both be implemented. However, GMG submits that multi-point balancing should not be considered at the expense of the MDV re-establishment implementation.

Cost Allocation

24. GMG supports the status quo and feels that no changes are required to the existing cost allocation methods.

Billing Terminology

25. GMG submits that harmonized terminology is critical for consumers. Both Enbridge and Union acknowledged in their oral testimony that there can be confusion with non-standardized terminology. The lack of consistency in the terminology used by the two utilities can be seen from the fact that both utilities preferred their own terminology over the others, as illustrated by Ms. Creery's statement that EGD would be "…happy to use our [the Enbridge] language." (2 Tr. 185, lines 12-22). If the billing terms used by each were truly synonymous, the utilities would be indifferent to which terminology was used.

26. While GMG is satisfied with any form of harmonized billing terminology, it prefers the terminology currently employed by Union.

Implementation Issues

27. The utilities have submitted that incremental operational costs will occur in moving to MRAM, but the cost drivers for each of the utilities differ significantly. Enbridge claims that increased incremental annual costs of $1.5 -$2.0 million are primarily driven by the need for additional staff required to repeat their "mechanistic" formula for rate setting 12 times per year rather than four, as well as incremental call centre costs. Alternately, Union Gas has stated that the incremental costs of moving to MRAM, which have risen from $1.6 million in their response to Board Staff IR #1 (Exhibit 1R24.1) to $2.45 million in Exhibit J1.1 (undertaking to CME) over the course of this proceeding, are primarily driven by the increased postage and insert costs due to a three page bill and $0.3 million from increased call volumes, meter reads and education.

28. The GMG believes that the OEB should not be deterred from making changes based on these admitted "high level estimates" of costs provided by the utilities for many reasons. The GMG has submitted evidence that the calculation for the Direct Energy Regulated Services (DERS) Gas Cost Flow-through Rate (GCFR) which is set on a monthly basis takes 10.55 person days to accomplish (GMG Evidence submission; Table 9; page 20). The utilities have criticized the applicability of this effort in Ontario, as it has not taken into consideration the storage and transportation requirements to serve the Ontario Market. However, Union has submitted in Union/GMG IR8.5, attachment #1 that the effort required to complete the QRAM is 15 person days. Furthermore, Enbridge agreed to this calculation (2 Tr. 56, line 8) by stating that "…they [Union] say 14 work days and we would agree with that." This would indicate that up to approximately 180 person days would be required to perform all 12 of the MRAM filings, which is the equivalent of less than one Full Time Equivalent (FTE). It would seem then that Enbridge's requirement for additional staff as detailed in the EGD response to the Board (EGD/Board IR#1) to move to a monthly rate setting mechanism is considerably overestimated and unreasonable.

29. Both utilities have also stated that incremental call centre costs will be incurred in moving to MRAM, but have failed to provide any foundation for their estimates. Customer calls related to the current QRAM are not tracked by either Union or Enbridge (2 Tr. 175, lines 14-18 and 1 Tr. 114, lines 19-23). However, this has not deterred Enbridge from asking the Board to believe an estimate of an additional 100,000 calls in perpetuity is reasonable. Nor has it deterred Union from requiring ongoing call centre costs of an additional $300,000 (Undertaking J1.1).

30. The GMG further questions why Union's incremental billing costs of approximately $1.4 million (Exhibit IR24.1) to move to MRAM should be accepted. Enbridge currently not only produces a 3 page bill, but also includes other parties on that bill, as well as additional third party inserts. Enbridge offers all of these additional services, yet is still able to manage the envelope weight within the 30 gram threshold set by Canada Post (2 Tr. 187, lines 2-9). Union, on the other hand, has provided no explanation as to why they are unable to meet this weight restriction.

31. In moving beyond the implementation cost estimates provided by the utilities for various proposals, it is important to recognize that the changes contemplated in this proceeding are for the betterment of all natural gas consumers in the province. Proper market structure decisions should initially be separated from the associated costs, so as to not unduly influence the appropriate decision making process. Ratepayers have been asked to bear the costs of implementations such as the new Enbridge CIS system, which have much larger price tags than those being contemplated here. Such a decision was made in the best interest of rate payers even though considerable costs would be incurred.

32. Approximately forty percent of natural gas customers in Ontario are Direct Purchase customers. As a result, it is important that all stakeholders including Marketers, consumers groups and the utilities be involved in the consultative process regarding the implementation and communication of any changes directed by the Board. To reiterate, the GMG supports Enbridge's proposal to allow the Board and stakeholders to determine an appropriate implementation approach.

Conclusion

33. The GMG believes that in order to provide the most accurate price signals to customers, the utilities should adopt a rate setting methodology that employs monthly price-setting, monthly forecasting and monthly dispositions. However, GMG understands that, for a variety of reasons, it may be more practical for the OEB to move towards this format in incremental steps.

34. As noted at the outset in this submission, the GMG believes that the evidentiary process in generic proceedings should allow for the debate and development of solutions that will be beneficial to

customers and market participants. The evidentiary process in such proceedings should not be used to continually entrench positions on either side, but should be a dialogue on how collectively stakeholders can continue the evolution and enhancement of the natural gas market in Ontario.

35. In this regard, the GMG would like to suggest a rate setting mechanism that is a compromise between the GMG position of a monthly filing using monthly forecasting and monthly disposition, and the utilities' position of a quarterly filing with 12 month forecasting and 12 month disposition.

36. In its pre-filed evidence, Union Gas objectively set out to determine if alternative scenarios could provide improvements over its current QRAM process. A better alternative was defined as "one that offers improved balance between price stability and market price sensitivity". By its own definition and supporting evidence, the GMG believes that Union has found a better alternative to its current QRAM methodology in "Scenario #1" as outlined on page 16 of Exhibit E2. This scenario provides for monthly rate setting with 12 month forecasting and a 12 month disposition of PGVA balances. This model results in almost exactly the same price stability, but with 21% greater accuracy.

37. While the GMG does not believe that this model is most reflective of market conditions, it is submitted as a good intermediate step that will better inform customers of the true cost of natural gas, and address the utilities concerns with respect to price volatility. Furthermore, a blending of the monthly price and gas taken from storage could better reflect the actual costs incurred by the utilities for the period as mentioned in the GMG's response to EGD Interrogatory #14.

38. From the perspective of the utilities, this scenario should be acceptable as it provides greater accuracy for their customers, along with a smoothing of the price which gives the appearance of more stability. In particular, it would address all of the concerns that Enbridge has with the GMG's MRAM proposal in paragraphs 14 to 18 of their Argument in Chief.

39. Furthermore, the GMG submits that the utilities have not provided any evidence to support their claim that customer confusion will occur as a result of moving to more frequent rate setting practices. If this were the case, the GMG suspects that the utilities would have provided such evidence as a result of the consequences of their move from the seasonal rate setting mechanism (SRAM) previously employed, to the current quarterly rate setting mechanism. The GMG would like to give Ontario consumers the benefit of the doubt in having the ability to understand more frequent price changes; considering both interest rates and gasoline prices change on a far more frequent basis than natural gas rates using the current QRAM process.

39. In closing, the GMG would to thank the Board once again for the opportunity to present its views on the issues in this proceeding, as well as for the Board's consideration in these matters.