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May 15, 2009

VIA COURIER and E-MAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
27th Floor
Yonge Street
Toronto, ON
M4P 1E4

Dear Ms. Walli:

Re: Board File No. EB–2008-0106
Commodity Pricing, Load Balancing, and Cost Allocation Methodologies for Natural Gas Distributors in Relation to Regulated Gas Supply

Please find enclosed VECC's submissions with respect to the above noted proceeding.

Yours truly,

Michael Buonaguro
Counsel for VECC
Encl.

VECC Argument
EB-2008-0106

Contents

1. These are the final submissions of the Vulnerable Energy Consumers Coalition, organized in accordance with the Issues List.

I Triggering Mechanisms

2. VECC agrees with Union and Enbridge that triggering mechanisms are no longer necessary. VECC therefore supports Enbridge's proposal to eliminate the existing triggering mechanism from its rate setting methodology.[1]

II Price Adjustment Frequency and Forecast Periods

Statement of Position

3. VECC believes that the approach proposed and currently used by Union, which Enbridge proposes to adopt, is appropriate. Under that harmonized approach base rates and riders related to gas costs would be adjusted quarterly based on forward-looking 12 month estimates of purchase gas costs and PGVA balances. The alternative methodology proposed by the Gas Marketer Group ("GMG"), VECC submits, would harm small-volume residential customers by increasing the volatility of overall utility sales rates and by impairing the ability of such customers to make informed decisions about their gas supply.

Description of Alternatives and Issues

4. The Utility proposal involves quarterly filings based on 12 month forward estimates of gas costs and PGVA balances. In substance, that mechanism generates sales rates (i.e. base rates together with riders) that reflect the best available estimate of the average cost of sales or system gas over the following 12 months.

5. The proposal set out in the GMG evidence was to re-set rates monthly based on some wholesale monthly index price, with PGVA balances cleared monthly over a one-month period. In its IR responses GMG modified this to provide for a blend of monthly index prices and historical inventory costs for storage volumes forecast to be delivered to customers during the winter months. Under this approach sales rates would reflect a blend of current monthly prices and a backward-looking accounting of the cost of

[1] VECC notes that Board Staff's submissions succinctly summarize the evidence with respect to trigger mechanisms at page 4 of their submissions, along with the rationale for the elimination thereof.

previously stored gas, with no forecast of the prices to be paid for gas, both for storage and immediate consumption, beyond the forecast month.

6. There is no suggestion that under either scenario the utility would be at risk for any gas costs, or that it would not continue to recover exactly its actual gas costs over time. There is also no dispute about the appropriateness of the utilities' current gas purchasing strategies. Any change in the methodology of deriving sales rates will therefore have zero effect on the average long run cost of system supply. The only issues relate to the pricing pattern under which the utilities' gas costs are recovered and the "price signals" that sales rates send to system gas users.

7. The proposals by the utility for a quarterly mechanism based on a 12 month forecast, incorporating both forecast prices and the costs of gas in supply, are based on and most closely match the one year cycle over which each utility purchases gas. In VECC's submission this methodology most closely reflects the costs of the utility in providing a monthly supply of gas to system gas customers, reflecting the utilities practice of drawing gas from storage, replacing gas in storage, and purchasing gas for immediate use. As explained by EGD:

   MS. GIRIDHAR: What we're referring to is the operational practice of procuring gas, and the reference is to the fact that gas is procured in a particular pattern over 12 months. We should keep in mind, if I may refer to your evidence, our understanding of that evidence was that you were recommending an approach whereby you would just reflect the monthly index based on what was consumed in a month as opposed to what was purchased in a month and we were drawing out the fact here that, in fact, we do have a purchasing pattern that is roughly constant over the 12 months. And the application of the 12 month price is reflective of that operational reality, in terms of how gas is procured.[2]

8. The need to provide pricing that matches the operational reality of the utility's purchasing pattern, particularly in terms of the role of storage in providing system gas, was ultimately accepted by the GMG when they altered their proposal to the Board during the IR process to account for the use of storage in pricing gas.[3]

9. Despite, however, taking this first step towards matching their proposal to the operational characteristics of the utilities' one year purchasing cycle, the GMG continue to resist the use of a 12 month forecast, instead continuing to propose monthly pricing based on a monthly forecast of price in support of their view of more accurate price signals with respect to the cost of natural gas.

[2] Transcript Vol. 2, pages 18-19.
[3] Transcript Vol. 3 page 48.

10. VECC supports and adopts Board Staff's submissions and summary of the evidence with respect to the analysis performed on the increased volatility caused by the GMG proposals and lack of evidence of improved price signals as a result of the GMG proposals, with the following additional comments with respect to price signals.[4]

11. With respect to the issue of price signals in the context of the differences between system gas and long-term fixed price gas sold by marketers in the residential market, VECC submits that there is an issue concerning the information available to consumers when making choices between the available services.

12. During the hearing EGD confirmed the types of information that a system gas customer can find, or be directed to if necessary, on their natural gas bill:

> MR. BUONAGURO: I just want to confirm or just clarify some things I heard already today.
>
> First of all, I was -- as I was listening to the first cross-examination, I pulled up on the Enbridge website a sample bill, just to take a look at what was being talked about. In particular, I was looking at how the prices show up on the bill, the price of gas is shown on the bill.
>
> My understanding is that on the bill, a consumer can look at the gas supply rate as a line item, and that rate is essentially the QRAM forecast, the most recent QRAM forecast for the next 12 months.
>
> MS. GIRIDHAR: Right.
>
> MR. BUONAGURO: So if a consumer is looking at the bill and wants to know what Enbridge's forecast of gas prices for that consumer is going to be in the next 12 months, they just have to look at that line item?
>
> MS. GIRIDHAR: That is correct.
>
> MR. BUONAGURO: Then the second part of the calculation on the bill is the gas cost adjustment which is just the rider?
>
> MS. GIRIDHAR: That's right.
>
> MR. BUONAGURO: Correct? And then you have the effective gas supply rate which combines the two?
>
> MS. GIRIDHAR: That is correct.
>
> MR. BUONAGURO: And if a consumer wants to look at their gas bill and find out how much they're paying per cubic metre of gas in that month, they just have to look at the effective rate; is that correct?
>
> MS. GIRIDHAR: That is right.
>
> MR. BUONAGURO: So at any point in time looking at your bill, you know what the gas forecast is from Enbridge's point of view over the next 12 months, but you also want to know how much you're actually paying for your actual consumption in the month that the bill represents.

[4] Board Staff Submissions, pages 5-10.

MS. GIRIDHAR: That is right. That is why we ensure that both of those items are shown separately but then also summed up in terms of the effective price.[5]

13. Accordingly a system gas customer can discern from their bill

    a) the utilities' forecast cost of system gas for the upcoming 12 months from the date of the last QRAM, and
    b) the actual, invariable, fixed price of natural gas that the customer will pay throughout the QRAM period covered by the combination of the current forecast price and gas cost adjustment.

14. VECC submits that all customers should be concerned about the relative overall costs of available options. All customers will want to know, to the extent they can, whether and by how much the overall cost of fixed-price gas can be expected to differ from variably priced system gas, recognizing that by definition the price of variably priced system gas is not guaranteed for any period.

15. Any rational customer weighing the relative merits of continuing with system gas or contracting for fixed-price supply will therefore be concerned about the likelihood that, over the term of the fixed-price contract, average utility prices will be lower than, higher than, or about the same as, the fixed price that is on offer.[6] Rational customers will not be interested in whether a proposed 1-year fixed price is higher or lower than next month's system price; they will want whatever information is available about whether on average they can expect to be better or worse off in the long run with the fixed price than they would be with the system price, and by how much.

16. The critical question here is that of what the Board's objective should be in relation to the market signals that are conveyed by sales rates. In VECC's submission the objective should be to convey to customers, to the extent possible, information that is relevant to the decisions customers have to make and that will assist them with making well-informed decisions that are consistent with their objectives and personal preferences.

17. VECC submits that the utilities have demonstrated that their proposals most closely match their respective gas purchasing cycles, such that, from that matching perspective, their proposals are the most appropriate. The question then becomes whether there is some material benefit to be derived from deviating from that matching principle in relation to the provision of a price signal to system gas customers.[7]

18. As explained above, probably the main issue on which customers faced with a choice between system gas and a fixed-price product want and need information is the likely

[5] Transcript Vol. 2, pages 63-64.
[6] See Transcript Volume 3, page 67, wherein the GMG panel agrees that consumers should be interested in the cost of sales service over as long a period as possible.
[7] See Transcript Volume 4, page

long-run relative cost of the two alternatives. By definition the long run average price of the variably priced system gas service cannot be known for certain, but that does not mean that it is not possible to estimate those costs at any point in time.

19. Sophisticated market participants like the utilities, marketers, and large industrial and commercial users in fact have access to forward market information that enables them to evaluate likely market outcomes and predict prices and costs under variably priced arrangements well into the future. It is precisely those tools that enable the utilities to produce the forecasts that are embedded in their sales rates. Similar tools are available to the marketers, as evidenced by the frequent references to and analytical use of forward prices in the GMG evidence, and to sophisticated end-users.

20. Those tools, however, are not available or useful to most residential customers. As a practical matter the only information available to typical residential consumers that is relevant to predicting the future price of system gas is the current system sales rate. While that may or may not be the best available information, it is a 12 month forecast of the price calculated to reflect the cost of system gas to system gas customers.

21. Sales rates designed using the Utility proposal would be, by design and definition, the best available estimate of the expected average cost of system gas over a forward one year period as of the time they are set. For a customer considering the options of system gas and fixed-price gas that is precisely the information that is relevant to making that choice. Under the utility proposal the prevailing system sales rate is therefore an appropriate and reasonable benchmark for customers to use in evaluating the reasonableness of fixed-price offerings.

22. To the extent that customers rely on sales rates calculated under the Utility proposal as indicators of future costs, that reliance will be well-founded and objectively reasonable, because sales rates calculated as proposed by the utilities will provide consumers with exactly the type of information that consumers need to make an optimal and well-informed choice of gas supplier. The fact that the forward-looking estimate embedded in sales rates at any given time will no doubt vary, as all forward-looking estimates do, and will accordingly be adjusted, does not change the fact that when the estimates are made they constitute the best available information about the likely future cost of system gas. They are therefore relevant and useful information for customers who want to evaluate fixed-price offerings.

23. In contrast, sales rates designed under the GMG proposal would have embedded in them no forward-looking information at all. They would therefore be, from an objective perspective, essentially useless to customers for the purpose of evaluating the likely future cost of sales service.

24. It appears from GMG's oral testimony that while they agree that

a) consumers should be interested in the long term forecast of system gas prices, and
b) the current pricing model used by the utilities provide such a forecast,

GMG suggests that the price represented on the bill should be restricted to the current month's projection of price as the appropriate reflection of the cost of that month's consumption. Accordingly, it appears to VECC, the GMG is asserting that the system gas price charge in a month should reflect the utilities system gas costs in that month, and that the utilities' proposals do not reflect those costs closely enough despite succeeding at providing the 12 month forecast.[8] Yet, as previously noted, the evidence from the utilities is that the pricing mechanisms they propose most closely match the costs associated with their 12 month operational cycle, and that even GMG, during the course of the proceeding, has had to augment its own proposal to better reflect the operational reality of how natural gas is purchased and provided to consumers through system gas.

25. Moreover, if and to the extent that customers nevertheless rely on current sales rates as a benchmark for competing fixed-price services, the short term and historical information reflected in rates designed using the GMG method would in many cases be not simply irrelevant to a proper decision, but misleading to customers.

26. Under the GMG proposal it is likely, as shown by Union's evidence, that system rates would periodically "spike" in response to seasonal factors, short term supply and demand disruptions, one-month recoveries of deferral balances, or simply random market movements.[9]If sales customers relied on prevailing sales rates during such periods as an indicator of future sales prices, as some would almost certainly do, those customers would perceive sales service to be much less attractive, relative to a competing fixed-price product, than they would if they had access to the same forward-looking information that the utilities and marketers have. Customers with access to only limited short-term information might easily be misled into entering into long term fixed-price arrangements that they would not enter into if they had more complete and accurate forward-looking information.

27. In effect the Utility proposal involves the utilities sharing with residential customers forward-looking market information that is available to more sophisticated market participants. The GMG proposal, on the other hand, appears to involve an attempt to ensure that such information is withheld from those customers most inclined to rely on that information. The information such customers would be given under the GMG proposal, VECC submits, would be at best irrelevant to the decisions they have to make, and at worst misleading.

[8] Transcript Volume 3 page 74 lines 12-14.
[9] Union Pre-filed evidence, page 19.

28. This sharing of information under the Utility proposal, which makes it possible for small unsophisticated customers to rationally evaluate the competitive alternatives that they have in the same way that the utilities, marketers, and large customers can, can be an enormous benefit to residential customers.

29. Lastly, VECC notes that the combination of a quarterly rate change, combined with rate certainty within the quarter, provides consumers with price certainty within each quarter, providing consumers with the ability to budget, based on price, within the period. For example, when the October 1 QRAM effective supply rate is announced, consumers on system gas know what their actual, immutable price will be for their gas consumption between October to December; when the January 1 QRAM price is announced, consumers are provided with an updated price signal in the middle of the heating season, by way of a new, certain price of natural gas to be charge from January to March. While it is true that the mew price will be affected by the variance between the previous forecast and actual prices experienced in the prior period, it does not change the price that was paid by consumers in the previous period as applied to their consumption in that period.

GMG Rationale for its Proposal

30. In order for the GMG to persuade the Board that its proposal should be adopted, VECC submits that the GMG must conclusively demonstrate that its scheme would involve some countervailing or offsetting benefit for residential customers, or some other group, that would outweigh the clear and significant benefits of the current pricing mechanism.

31. In VECC's submissions GMG has been unable to do that. The basic theme of the GMG evidence is that utility sales prices should reflect short term monthly pricing, essentially because the utilities themselves purchase gas on a monthly basis at monthly prices. This basic proposition is repeated in a number of places in a number of forms.[10] What is never provided, however, is an explanation of why it is necessary or desirable, from the perspective of sales customers or anyone else, to design sales rates on the basis of monthly prices to match the monthly prices paid by the utilities.

32. While there are vague allusions to "appropriate price signals", there is no discussion of what constitutes an appropriate price signal in this context or why it is important, who would benefit from an appropriate price signal, or why. The evidence makes no attempt to show that adopting GMG's proposal would provide unsophisticated residential customers with better or more relevant information than the Utility proposal would. With the exception of a few minor and unpersuasive hints or asides, which are discussed

[10] For Example, Evidence of the GMG, page 8.

below, the GMG evidence makes no serious attempt to justify the GMG proposal or explain why it would benefit residential sales customers.[11]

33. VECC notes that when confronted with the example of the BCUC's decision to retain quarterly rather than monthly adjustments, the GMG panel dismissed the example as irrelevant as a result of the lack of a competitive market in that jurisdiction:

MR. CASS: Right. Thank you. Am I right in thinking that the BCUC had also decided in favour of quarterly rather than monthly adjustments?

MR. NEWCOMBE: Yes. I think you have to look at the context. That BCUC letter was written back in 2001, so there was no open competitive retail market at the time. If there's only one choice and you're working on flow-through gas, it probably doesn't matter how often you reset the rates.

34. In VECC's submission this exchange makes clear that the GMG panel is primarily concerned with the effect of the pricing mechanism on the volatility of system gas relative to the fixed price contract market, and not on the price signals transmitted to system gas customers as a result of the manner in which system gas is priced. If the latter was of concern, then GMG would have had to acknowledge that the BCUC and the OEB are both engaged in gauging the price signals experienced by consumers, and in that engagement the BCUC recognized that a quarterly pricing mechanism for natural gas supply struck an appropriate balance between volatility and appropriate price signals. VECC submits that, in fact, it may well be that where system gas is, as it was in the case of the BCUC decision, the only offering, it becomes the only, and therefore most important price signal, and yet was still calculated on a quarterly basis under the BCUC regime.

"Informed Consumption Choices"

35. At various points GMG claims that its proposal for monthly pricing would enable consumers to "make more informed ... consumption choices" .[12] While this is never explained or justified, on the basis of expert economic evidence or otherwise, the suggestion appears to be that monthly pricing will somehow lead to more efficient gas consumption behaviour by consumers.

36. In response to this possible suggestion we would make several points. First, if GMG wants to rely on a theoretical economic proposition as a justification for its proposal it needs to state that clearly and support the proposition with real evidence. Second, even assuming that in principle short term price levels could influence consumer behaviour in some way, GMG makes no attempt to show empirically that they do so in the residential gas market, or that any such effect is material. Finally, any suggestion that variable

[11] Board Staff submissions, at page 10 similarly make note of the lack of evidence concerning price signals and the effect on conservation behaviour.

monthly pricing leads to socially desirable outcomes by influencing consumer consumption behaviour is inconsistent with GMG members' own business model of fixing prices for 1-5 year periods. If residential sales customers should be forced to accept wildly fluctuating monthly rates in pursuit of a social efficiency goal, then five-year fixed price contracts must necessarily be prohibited outright.

"Facilitate Provider Choice"

37. In conjunction with its references to "informed consumption choices" GMG usually refers to "informed provider choice" or "facilitating provider choice". If the suggestion is that sales rates should be designed with the simple objective of making them look as different as possible from marketer prices, VECC submits that such is not an appropriate design criteria for system gas pricing.

38. In VECC's submission, continuing the utility proposal facilitates informed provider choice by giving residential customers information that is relevant and useful for the purpose of making a rational choice between system gas and fixed-price supply; by contrast, the GMG proposal would make that choice more difficult by depriving customers of that information.

Intergenerational Issues

39. At various points in its evidence and IR responses GMG makes various comments and observations to the general effect that its' proposed rate-making methodology would result in more accurate forecasts and, as a general matter, smaller deferral balances. This is coupled with the claim that smaller deferral balances are desirable because they minimize any mismatch between the customers for whom costs are incurred and those from whom they are recovered.

40. It may be true that as a general matter the GMG approach would result in smaller deferral balances, largely because the underlying market variability would be captured in base forecasts rather than deferral accounts. This does not, however, change the underlying variability, however, and as a general matter it appears that variability in overall rates, i.e. base rates and riders, would be at least as great, and probably greater, under the GMG approach than under the Utility approach.

41. With respect to the claim that it would be desirable to minimize deferral balances in order to minimize intergenerational "mismatches", GMG presents no evidence in relation to the size or severity of any such mismatches, so cannot claim that they are material, nor does it present any evidence to suggest that the utility proposal would involve or create a systematic bias that would disadvantage any particular group of customers.

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[12] Evidence of GMG, page 4, last paragraph.

42. In principle it is true that under a QRAM system some customers may avoid paying their share of a large debit balance brought forward from a previous quarter by switching to fixed-price supply. On the other hand, some customers may end up paying debit balances from a previous quarter by returning to system supply. Equally, some customers may miss out on the benefit of a credit balance by switching to marketer supply, or receive the benefit of such a balance by returning to system. Such effects, experienced to a greater or lesser degree, are an inherent feature of all rate-making systems that utilize deferral accounts, including the DERS regulated supply mechanism in Alberta. Without a demonstration that they give rise to a material systemic unfairness problem in the context of the Utility proposal, the mere fact that such effects may arise is not sufficient to outweigh the advantages of the Utility proposal have been identified.

Summary

43. In summary VECC submits that the Utility proposal in relation to the design of system sales rates is clearly superior to the GMG proposal. In VECC's view the GMG proposals would unjustifiably degrade the utility supply option. As GMG agreed in cross examination:

MR. CASS: Okay. Well, I wasn't -- sorry if I misled you into thinking the question had anything to do at all with the Manitoba decision. The question was just to confirm your view and the view of this panel, in fact, that it would not be appropriate for this Board, the Ontario Energy Board, to do something simply to make system gas so unattractive that people would move off of system gas.

MR. NEWCOMBE: No. I don't think that should be one of the criteria that the Board uses for their decision-making as a relative attractiveness or unattractiveness of any of the offerings, no.

III Methodology for Calculation of Reference Prices

44. VECC does not believe that it is necessary to provide for a single reference price for Ontario, for the reasons outlined by the Utilities in their evidence and arguments. A single reference price, in VECC's view, is meaningless if it does not , in fact, reflect the price that is going to be provided by the utilities. While in theory it could be desirable for the system supply option to be uniformly priced across Ontario, similar to how the Regulated Price Plan option is provided to electricity consumers, VECC submits that the realities of the different procurement and operational options available within the Union and Enbridge franchise areas appear to prevent this option from being realized.

45. With respect to Questions 3.2-3.4, VECC generally supports the Utility proposals.

IV Deferral and Variance Accounts and Disposition Methodology

46. VECC supports the harmonized proposals advanced by the Utilities.

V Effect of a Change in the Reference Price on Revenue Requirement

47. Union proposes to adopt Enbridge's practice of updating its revenue requirement and non-gas rates quarterly. VECC supports this proposal.

VI Implications/Costs of Standardizing Pricing Mechanisms Across all Distributors

48. With the changes proposed by Union and Enbridge to harmonize their pricing mechanisms, and without considering changes in service structures, further standardization is not necessary at this time.

VII Filing Requirements

49. It appears to VECC that the QRAM applications of Union and Enbridge are quite different and, to the extent possible, would benefit from standardization. In VECC's view Enbridge provides more detail on supply volumes and unit prices by supply point than Union, and accordingly VECC submits that Union should provide similar detail. If such detail is not helpful, we ask that Union explain why in reply argument.

VIII Load Balancing

50. VECC supports the utilities proposals with respect to this issue.

IX Cost Allocation

51. With respect to the allocation of utility operating costs between direct purchase fees and system supply fees, VECC supports the current approach.

52. Issues that can generally be classified as related to cost allocation also arise in relation to the allocation of transportation and non-Alberta supply costs between various functions and customer classes. It is difficult to compare the main utilities because they

offer quite different services, i.e. Enbridge offers a Western Bundled T while Union does not. In its IRs VECC explored differences between Enbridge and Union in relation to the allocation of “Empress/TCPL” costs versus “Overall Portfolio” costs between, effectively, sales and DP customers. It appears that Union sales customers ultimately pay rates that reflect the cost of Union’s overall portfolio, while Enbridge sales customers ultimately pay rates that reflect the cost of Empress/TCPL supply and transportation, with variances between those unit rates and unit rates implicit in Enbridge’s overall supply portfolio allocated across all customers via a balancing charge.

53. While in principle this seems like a significant conceptual difference, and as a general matter VECC believes that the Union approach makes more sense, we do not believe that it would be appropriate to make changes through this proceeding.

54. First, we are satisfied that the practical difference for Enbridge between the two conceptual approaches is negligible. If Enbridge’s supply and transportation portfolio changed significantly it might be necessary to revisit the issue.

55. Second, the differences that exist between Union and Enbridge appear to relate fundamentally to differences between the DP services that the two companies offer, and in particular to the fact that Enbridge’s services, i.e. its Western Bundled T, are not unbundled to the extent that Union’s is. Our understanding is that issues related to further unbundling of Enbridge’s services will be addressed in a separate proceeding, and any changes in Enbridge’s service structure would inevitably involve an examination of the cost allocation issues we have identified. It is therefore premature to consider those issues here, and they should be left to the broader consideration of unbundling Enbridge’s services.

X Billing Terminology

56. In VECC’s submission, while there may be some utility in standardizing the language between the two utilities, the critical point is that customers encountering their own bill are provided with enough information to understand the presentation to them. Similarly, VECC’s concern with Billing Terminology is not so much which, of the two ways, it is done, but rather that the parties who may use Billing Terminology during the course of explaining or marketing gas supply options to consumers do so accurately and fairly.

XI Implementation Issues

57. VECC has no comments, and generally supports the Utilities.

COSTS

48. The Vulnerable Energy Consumers Coalition hereby requests that the Board order payment of our reasonably incurred costs in connection with our participation in this proceeding. It is submitted that the Vulnerable Energy Consumers Coalition has participated responsibly in all aspects of the proceeding, in a manner designed to assist the Board as efficiently as possible.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 15TH DAY OF MAY 2009