



***PUBLIC INTEREST ADVOCACY CENTRE***  
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January 09, 2012

**VIA MAIL and E-MAIL**

Ms. Kirsten Walli  
Board Secretary  
Ontario Energy Board  
P.O. Box 2319  
2300 Yonge St.  
Toronto, ON  
M4P 1E4

Dear Ms. Walli:

**Re: EB-2010-0018**  
**Natural Resource Gas Limited – 2011 Gas Rates Application Phase 2**

Please find enclosed the final submissions of the Vulnerable Energy Consumers Coalition in the above noted matter.

Thank you.

Yours truly,

Michael Buonaguro  
Counsel for VECC  
Encl.

**ONTARIO ENERGY BOARD**

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

**AND IN THE MATTER OF** an Application by Natural Resource Gas Limited to the Ontario Energy Board for an Order or Orders approving or fixing just and reasonable rates and other charges for the sale, transmission and distribution of gas as of October 1, 2010.

**AND IN THE MATTER OF** an Application by Natural Resource Gas Limited for an Order or Orders approving a multi-year incentive rate mechanism plan.

**FINAL SUBMISSIONS OF THE VULNERABLE ENERGY CONSUMERS COALITION**

**JANUARY 09, 2012**

**APPROPRIATE PRICING OF GAS PURCHASED FROM NRG CORP**

NRG Ltd. ("NRG") proposes to pay a floor price of \$8.486 per mcf for all volumes of gas bought from the related entity NRG Corp. whenever the market price for gas is \$9.9999 per mcf or less and market price for gas when said price is \$10.00 per mcf or more.<sup>1</sup>

With respect to removing, from NRG Corp., all downside price risk when the market price falls below \$8.486, NRG has stated that there is, in its proposal, a mitigating upside for ratepayers: when the price exceeds the floor but remains below \$10.00, ratepayers will pay less than market price.<sup>2</sup>

There is no minimum or maximum volume specified in the arrangements between the utility and NRG Corp.; NRG Corp. provides whatever volumes are requested by the utility.<sup>3</sup>

VECC notes that NRG Ltd., the utility, is currently the only customer for NRG Corp.'s gas commodity sales business.<sup>4</sup>

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<sup>1</sup> NRG Ltd. Argument in Chief (AIC), paragraph 74.

<sup>2</sup> Ibid, paragraph 75.

<sup>3</sup> Transcript, November 30, 2011, page 32

<sup>4</sup> Transcript, November 30, 2011, page 30

As to how the price specified was determined, VECC submits that the details of the “calculation” are vague at best.

At one point during the oral hearing, the following explanation was provided by the witness:

*MR. MILLAR: The September 30th letter is the letter that sets out the price that NRG is prepared to provide gas for. Do you see that?*

*MR. GRAAT: That's correct.*

*MR. MILLAR: How did you set on this price?*

*MR. GRAAT: There's a number of factors; it's primarily it costs X number of dollars to drill a well and to finance and to inventory it, and to make sure it works and to do a number of things. And we thought -- we believe that that is the price that we need, which is similar to the price that we were receiving prior to the price of gas, which comes from TransCanada, has been lowered dramatically.*

*MR. MILLAR: Do I understand you to say that this price is more or less what is required to recover your costs?*

*MR. GRAAT: From our point of view. From NRG Corp.'s point of view.*

*MR. MILLAR: I presume cost would include a rate of return or something like that, as well?*

*MR. GRAAT: That's correct.<sup>5</sup>*

VECC notes that the above factors listed by NRG's witness as inputs to the minimum floor price appear to be mainly sunk costs, i.e., costs that have already been incurred and that will remain, regardless of future decisions made by the company.

Furthermore, VECC notes that the record with respect to what prices were charged, when, and why, is muddy.

*MR. BUONAGURO: I'm trying to figure out when that number came into effect and how it did. And so the answer I first got was, the methodology changed in 2006. Then I got an answer that said, well, yes, the methodology changed, but that's not the number that*

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<sup>5</sup> Ibid, pp. 22-23

*it required. Then I got, it was the average price over the year. And then I got, well, actually, there was a point in time where the methodology actually spit out that price. So as may be understandable, I'm a little bit confused about what actually happened, but I'm just trying to nail down -- the answer we're getting from NRG Corp. is that that's the price we need in order to not suffer a loss. That's the price we need in order to pay -- to recover our costs of the gas with the included ROE, and anything less than that, we're going to shut down the wells.*

*MR. KING: I understand that.*<sup>6</sup>

VECC also notes that this is a very unusual situation in a number of respects: (i) the sole buyer for NRG Corp.'s gas is a related utility; (ii) unlike other arrangements, the related party is selling commodity gas to the utility at a premium; and (iii) NRG Corp. is guaranteed a floor price, regardless of how low comparable market prices become.

The utility also stated that comparable prices for NRG Corp. supplied gas should add a transportation premium to the hub market price; VECC submits that it is equally valid to look at what price – net of transportation charges – NRG Corp. could sell its gas at Dawn as a comparator.

VECC submits that it is in general inappropriate to set floor prices paid by a utility to an unregulated related party that guarantee – up to a point – a premium above market prices. VECC further submits that the ‘negotiations’ between NRG Ltd. and NRG Corp. appear to have been dominated by the unregulated party’s take-it-or-leave-it offer, with the utility having very little latitude in the talks; the outcome does not seem to be the product of a fair bargaining session.

In this instance, VECC believes that the floor price is indicative of market power, exercised by a dominant or critical supplier to the utility.

VECC’s view is that in the short run, any floor price that is demanded by NRG Corp. should be fully supported by financial details that could establish that it would not be in NRG Corp.’s financial interest to ever supply below that floor price – before getting regulatory approval.<sup>7</sup> In VECC’s view, this has not been established with respect to the current proposed floor of \$8.486 and a market-based methodology should be preferred.

To that end, VECC supports the recommendations of Board Staff, that, in the absence of an appropriate RFP process (as described below), the Board should continue to implement the current Board approve pricing methodology.

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<sup>6</sup> Ibid, pages 112-113

<sup>7</sup> This presumably would be confidential.

## **THE NEED FOR AN RFP**

NRG Ltd. Has stated that it has 41 wells in its franchise area<sup>8</sup> as compared to “thousands of wells in the franchise area.”<sup>9</sup>

VECC submits that the testimony given at the oral hearing indicated that the utility has made little to no effort to determine if there is any interest, from the owners of these thousands of wells, in supplying commodity to the utility.

VECC submits that the Board should direct the utility to undertake a public process to determine the level of interest of these potential suppliers of gas commodity. The process should be well advertised and should state the utility’s reasonable terms of reference for any expressions of interest.

Lastly, VECC submits that the utility should be required to report to the Board on the process undertaken and the outcome of the process in 12 months from the date of the decision in this case.

## **THE NEED FOR ANOTHER INDEPENDENT ENGINEERING STUDY**

During the oral hearing, the utility’s technical witness gave testimony that indicated: (i) that the system integrity study did not include a sensitivity analysis;<sup>10</sup> (ii) the study could not tell how much integrity was required or when it was required;<sup>11</sup> (iii) the study assumed that only five wells were turned on;<sup>12</sup> (iv) the author of the study did not discuss with Union any other possibilities;<sup>13</sup> and (v) the study did not consider the possibility of any wells, other than the five, being turned on.

VECC submits that a system integrity study of wider scope is required, a study that would involve robust sensitivity analyses, and that would give consideration to all possible alternatives to the current NRG Corp. status quo arrangement. VECC urges the Board to direct the utility to commission an independent expert to undertake such a study.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 9<sup>th</sup> DAY OF JANUARY 2012**

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<sup>8</sup> Ibid, page 17

<sup>9</sup> Ibid, page 118

<sup>10</sup> Ibid, page 82

<sup>11</sup> Ibid, page 83

<sup>12</sup> Ibid

<sup>13</sup> Ibid, page 89