

By electronic filing

December 31, 2012

Kirsten Walli
Board Secretary
Ontario Energy Board
27th floor – 2300 Yonge Street
Toronto, ON M4P 1E4

Dear Ms Walli,

Union Gas Limited (“Union”)	
2013 Rebasing Application	
Board File No.:	EB-2011-0210
Our File No.:	339583-000123

As solicitors for Canadian Manufacturers & Exporters (“CME”), we are submitting below our comments on the Draft Rate Order (“DRO”) and supporting materials that Union circulated on December 13, 2012.

A. Context

1. Complexity of the DRO

As a preliminary observation, we found the task of working through the text of the DRO, its Appendices, and its 46 Schedules of Working Papers to be a challenging exercise. This task was ameliorated to some extent by the further material and explanations provided to us by Mr. Kitchen and Mr. Ripley.

Our goals in examining the DRO were:

- (a) To first understand and attempt to quantify the causes for the changes that have occurred to the level of rates and charges in each of Union’s North and South operations areas as a result of the Settlement Agreement and the Board’s Decision and Order dated October 25, 2012 (the “Reasons”) compared to Union’s initial filing; and
- (b) To determine in what respects the DRO might need to be revised to reflect the intent of the Reasons.

2. DRO Rate Impacts

Of concern to us are the wide range of rate impacts for different rate classes that appear in Schedules 15, 16 and 17 of the DRO Working Papers.

For example, Schedule 17 shows that percentage changes in “Delivery Charges” in the North range from an 11.5% increase for Small Rate 01 to a 50.5% increase for Large Rate 20. In the South, the percentage

changes in “Delivery Charges” range from a decrease of 26.4% for Large Rate T2 to a 40.3% increase for a Large Rate M5 customer. Within the former T1 class, the percentage changes range from a decrease of 26.4% for Large Rate T2 to an increase of 30.8% for Small Rate T1 customers.

We appreciate that these changes are to the “Delivery Charges” components of rates and do not include what Union includes as “Gas Supply Charges” in these rate impact Working Papers and assume that “Delivery Charges” in Schedule 17 includes everything other than the “Gas Supply Charges” Union recovers in its rates. That said, there are many customers who acquire delivery services only from Union and for whom the total bill from Union will materially increase under the DRO.

In these circumstances, we submit that it is in the interests of all stakeholders that there be a clear understanding of all of the major “rebasings” factors that are acting in combination to produce this outcome.

The “rebasings” factors that we believe are acting in combination to produce the rate impacts reflected in the DRO include:

- (a) The rebasing of the system-wide revenue requirement to reflect Board approved forecasts of 2013 revenues, expenses, rate base and return;
- (b) The rebasing of the allocation of the system-wide revenue requirement to reflect current information related to the derivation of the applicable cost allocation factors;
- (c) The requirement that Union allocate revenues that it realizes from transactional services on a basis that reflects sound regulatory principles;
- (d) The rebasing of all class rates to better align their levels with allocated costs; and
- (e) The revision of rates within the former T1 class to make them more cost-related.

In its response to comments on the DRO, Union should provide a complete list of these factors, along with a high level estimate of their impacts on rates in the North and South.

3. Need for a Narrative Describing the Drivers of DRO Impacts

We submit that the DRO needs to be accompanied by a written narrative that summarizes and quantifies at a high level the drivers of the DRO rate impacts. In our view, Union’s December 13, 2012 letter that accompanied the DRO fails to achieve this objective because it does not link all of the main causes of the rate changes to the “Delivery Charges” displayed in Schedule 17 of the Working Papers.

In this connection, we request that, in its response to comments on the DRO, Union include a written narrative that summarizes and explains the major factors that are acting in combination to produce the total revenue requirement being allocated and recovered from the North and the South respectively.

4. Allocated Revenue Requirement Drivers of DRO Impacts

The foregoing narrative should identify the total revenue requirement that Union initially asked the Board to approve, including its allocation between the North and the South. The narrative should then identify the total amount approved and allocated between North and South with those amounts separated between their delivery-related and gas supply-related components.

Our understanding is that one of the major reasons that rates are increasing in the North is because total usage in that area has not kept pace with the increased costs to serve those customers. If there are other major factors stemming from the Reasons that results in more costs being allocated to the North than Union proposed in its initial filing, then we submit that these items and their affect should be described in the written narrative that we are proposing.

To illustrate the problem that we are experiencing in reconciling the DRO “Delivery Charges” impacts shown in Schedule 17 with other information in the Working Papers, we start with the as filed revenue deficiency of \$71.318M shown at line 13 of column (a) on page 1 of Schedule 1. As a result of our discussions with Union representatives, we understand that this amount is the net of a delivery-related deficiency of about \$73.083M (i.e. all amounts other than “Gas Supply Charges”), and a gas supply sufficiency of \$1.765M.

We further understand from our discussions with Union representatives that, as a result of the Settlement, the delivery-related component of the total deficiency declined by about \$14.8M to an amount in the order of \$58.2M.

We believe that there should be a further decline in the total delivery-related deficiency as a result of the Board’s findings in the Reasons. This belief is reinforced by communications with Union representatives who point to lines 6, 16 and 17 on page 1 of Schedule 11 in column (f), which show the delivery-related deficiency at the time of settlement declined by a further \$16.647M. This then should reduce the total settlement delivery-related deficiency of about \$58M to an amount of almost \$42M.

The problem we are having is reconciling all of this information with the information presented at Schedule 10 of the Working Papers. Schedule 10 at line 11 indicates to us that the total deficiency being recovered in rates as a result of the reasons is \$12.039M. The components of this amount are a delivery-related deficiency of \$56.453M shown at line 9 and a gas supply-related sufficiency of \$44.414M shown at line 10. Moreover, the delivery-related deficiency being recovered in the North at line 5 appears to be \$72.265M, whereas the delivery-related sufficiency shown in lines 6, 7 and 8 appears to be an amount slightly less than \$16M.

It is unclear to us how the outcomes presented in Schedule 10 are linked to the Reasons. We suggest that what is needed to clarify these matters is a narrative that links the DRO rate impacts to the major findings in the Reasons, and this is why we suggest that Union provide such a narrative in its response to comments on the DRO. If we are misinterpreting any of the information contained in the Working Papers, then the narrative that we are requesting will clarify the manner in which the information should be interpreted.

5. Rate Design Drivers of the DRO Impacts

On the Rate Design front, we suggest that it would help stakeholders better understand the DRO if the narrative describes the major features of the Reasons that are causing the broad range of delivery-related impacts shown in Schedule 17 of the Working Papers. On that score, we understand that the Board’s rejection of Union’s proposal to use forecast Base Exchange revenues to reduce rates in the North is one factor that is prompting increases in all delivery rates in the North compared to Union’s initial filing.

In the South, we understand that the combined effect of approving Union’s subdivision of the former T1 class into new T1 and T2 rate classes produces the significant increases and decreases in rates to customers within the former T1 class, despite the reduced recoveries from the former T1 class and increased recoveries from other classes to make rates of all classes in the South more cost-related.

These and any other major Rate Design drivers of the DRO Impacts should be described by Union in the narrative that we are proposing.¹

B. Specific Comments on the DRO

(a) Page 4 (c) entitled “Optimization Margin”

This section of the DRO stems from those findings in the Reasons at pages 35 to 42 within the major section entitled “Optimization and Gas Supply Plan”. This section starts at page 25 of the Reasons.

In the DRO, Union is interpreting the findings in the Reasons at pages 39 and 40 to require that revenues realized from optimizing assets, other than Union’s upstream supply portfolio held to serve its in-franchise bundled customers, be classified as Gas Supply with 90% thereof to be held for the benefit of ratepayers as Gas Supply cost reductions.

We question whether this is the appropriate interpretation of the Board’s Reasons.

The evidence at the hearing indicated that Union engaged in optimization activities using assets outside of the ambit of its upstream supply portfolio held to serve in-franchise customers. Assets used to support such optimization activities included Union’s integrated transmission, storage and distribution assets, with or without incremental upstream transportation that Union acquired outside of the ambit of its Gas Supply Plan to support such transactions. These optimization activities that take place outside of the ambit of the Gas Supply portfolio held by Union to serve its in-franchise customers include “Base Exchanges”.

In the Reasons at page 39, the Board accepted Union’s definition of Gas Supply portfolio “optimization” which is confined in scope to the optimization of the Gas Supply portfolio that Union holds to serve its in-franchise bundled customers.

The incremental upstream transportation that Union acquires to support “Base Exchanges” that in turn depend upon the existence of Union’s other integrated assets is not part of the Gas Supply portfolio that Union holds to serve its in-franchise customers. The amounts that Union spends on incremental upstream transportation to support “Base Exchanges” are not charged to ratepayers through any Gas Supply Deferral Accounts. They are third party costs incurred to support optimization activities unrelated to the Gas Supply portfolio that Union holds to serve in-franchise customers. It follows that “Base Exchanges” do not fall within the ambit of the definition of Gas Supply portfolio “optimization” that the Reasons adopts.

Having regard to the foregoing, we believe that the Gas Supply Variance Account described in the Reasons at the bottom of page 39 is limited in scope to “optimization” activities in which Union engages using the upstream transportation it holds to serve its in-franchise customers.

We believe that other “optimization” activities, including the revenues from “Base Exchanges” net of all third party costs, including incremental transportation acquired outside of the ambit of Union’s Gas Supply Plan, are to be brought into revenue requirement, as the Reasons state at page 40, and allocated to rate classes in the North and South on the basis of sound regulatory principles.

Net revenues from the “optimization” of assets other than the upstream gas supply portfolio that Union holds to serve its in-franchise customers should be classified and allocated on the basis of sound

¹ The Revenue Requirement Change by Rate Class shown in Schedule 6 of the Working Papers does not help us understand the DRO rate impacts.

regulatory principles. We understand that these assets are paid for by all ratepayers through their delivery rates and, accordingly, the benefits of these “optimization” activities should flow to all ratepayers.

Union’s classification of the \$9.1M of forecast “Base Exchange” revenues for 2013 as a Gas Supply-related amount to be allocated only to those rate classes who pay for the Gas Supply portfolio that Union holds for in-franchise customers is, we submit, incompatible with the definition of Gas Supply portfolio “optimization” adopted in the Reasons. The \$9.1M of forecast “Base Exchanges” revenues should be treated differently than the Gas Supply portfolio “optimization” margins.

With these comments in mind, we submit that this section of the DRO and other related provisions need to be revised. We suggest the following revisions.

- Change the heading on page 4 that currently reads “Optimization Margin” to read “Upstream Gas Supply Optimization Margin”
- Change the first paragraph under this heading on page 4 of the Reasons to read as follows:

“In its EB-2011-0210 Decision, the Board ordered the establishment of a new Gas Supply Variance Account in which 90% of ~~the~~ Upstream Gas Supply Optimization margin not otherwise reflected in the revenue requirement ~~are~~ is ...”

- On page 5, before the text that reads “The Board therefore orders that ...” add a new section, (d) entitled “Base Exchange Revenues” to specifically address the 2013 Base Exchange revenue forecast of \$9.1M referenced in the Reasons. We suggest something to the following effect:

“(d) Base Exchange Revenues

In the EB-2011-0210 Decision, the Board directed Union to reflect 90% of its 2013 forecast of Base Exchanges of \$9.1M in its 2013 revenue requirement and to allocate that amount to rate classes on the basis of sound regulatory principles ...”

The text in this new section should describe how Union proposes to allocate the \$9.1M of Base Exchanges to rate classes on the basis of sound regulatory principles, having regard to the fact that revenues from Base Exchanges are not an outcome that stems from Union’s optimization of the Upstream Gas Supply portfolio that it holds to serve in-franchise bundled customers.

- As a consequence of the foregoing, paragraph 25 on page 9 should be revised to change the phrase in lines 1 and 2 “... revenue from optimization activities ...” to read “... revenue from Upstream Gas Supply Optimization activities ...”. Similarly, in paragraph 37 on page 11, the Gas Supply Optimization Deferral Account should be limited to recording 90% of Upstream Gas Supply Optimization margins not reflected in the revenue requirement.
- The wording of Deferral Account 179-131 should be revised to confine its application to Upstream Gas Supply Optimization margins.
- An additional paragraph needs to be added to the proposed DRO to deal with Base Exchanges in the manner described above.

C. Mitigation Measures

The DRO is based on a premise that no rate mitigation is necessary.

We question whether this premise is appropriate when there are many customers in several rate classes that will be facing increases in their delivery charges that are well in excess of 10%. The Customer Notices that Union asks the Board to approve at Appendix D of the DRO quantify the average delivery rate increases/decreases for contract customers as follows:

- Rate 20 47.8%
- Rate 25 30.6%
- Rate 100 30.2%
- Rate M4 15.5%
- Rate M5A 37.6%
- Rate M7 12.3%
- Rate M9 11.3%
- Rate M10 105.4%
- Rate T1 22%
- Rate T2 (22.5%)

We accept that for non-contract customers, Total Bill Impact should be the primary guide for determining whether mitigation measures should be adopted, however, for contract customers, the situation is different because many of them only pay Union for delivery services. For many customers, their costs of Gas Supply are the subject matter of a separate bill.

In prior cases, the Board has considered the magnitude of delivery-related charge increases only in determining whether large percentage rate increases and off-setting decreases should be phased-in as a mitigation measure. Phase-in periods of up to five (5) years have been adopted in prior cases.²

We urge the Board to consider whether a phase-in of the increases and decreases in contract rates over a period of two or more years is needed for non-contract customers, having regard to the range of delivery charge impacts disclosed in the DRO Working Papers.

² A phase-in period of five (5) years was approved by the Board to hold the delivery rate impacts of adversely affected customers of Enbridge Gas Distribution Inc. (“EGD”) to less than an annual increase of 10% when EGD adopted a new method of allocating Upstream Transportation Demand Charges to its customer classes.

Similarly, Union’s Delivery Commitment Credit was phased-out over a period of years to limit the delivery-related impacts on adversely affected customers to amounts considerably less than 10% per year.

D. Customer Notices

The Board has repeatedly stated that one of its priorities is to assure that utility customers are better informed about their energy bills. In this context, we urge the Board to carefully review the Customer Notices that Union asks it to approve.

Because the rate impacts in this case vary widely from customer to customer and are the outcome of this rebasing proceeding that follows five (5) years of rate setting under the auspices of an Incentive Rate Mechanism ("IRM"), these Notices need to contain sufficient information to enable each customer to understand why the rates are changing to the degree that they are, particularly in those cases where the rates for customers are increasing significantly.

The text of the draft Notices that Union has prepared for its contract customers does little, if anything, to help them understand the causes for the rate changes that the Board has approved. The text of these Notices should be strengthened in order to convey that information to all contract customers and particularly those whose rates are increasing significantly.

The narrative we are proposing should help the Board and its staff work with Union to develop Notices that will inform customers of the major causes for the level of rate changes that the Board has approved.

Yours very truly,

"Signature on Original"

Peter C. P. Thompson, Q.C.

PCT\slc

c. Chris Ripley (Union)
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