January 8, 2013

Ontario Energy Board
2300 Yonge Street
Suite 2700
Toronto, Ontario
M4P 1E4

Attention: Ms. Kirsten Walli, Board Secretary

RE: EB-2011-0210 – Union Gas Limited – 2013 Rates Application
Draft Rate Order Reply Comments

Union Gas Limited ("Union") filed its EB-2011-0210 Draft Rate Order on December 13, 2012 following the Board's Decision and Order dated October 25, 2012. Union received comments from Board Staff, the London Property Management Association ("LPMA"), the Canadian Manufacturers and Exporters ("CME") and one customer, Atlantic Power Limited Partnership ("APLP").

The following are Union's reply comments.

Draft Rate Order ("DRO") Comments

LPMA

LPMA's submission dated December 28, 2012 states that "Union has appropriately and adequately reflected both the Board's Decision and Order dated October 25, 2012 and the revised Settlement Agreement as filed on July 24, 2012 and approved by the Board on July 25, 2012".

LPMA notes that the effective billing date on page 2 of the DRO is incorrect and should read January 1, 2013. Union agrees.

Board Staff

Board Staff's submission dated December 31, 2012 supports the DRO as filed including Union's proposals for the allocation of storage and transportation margins, gas supply optimization margins, the elimination of rate classes Rate 77, U5, U7, U9 and the unbundled storage service offerings on the Rate 20 and Rate 100 rate schedules.

Board Staff requested that Union comment on Staff's submission regarding two accounting orders: Short-term Storage and Other Balancing Services Deferral Account (No. 179-70) and Upstream Transportation Optimization Deferral Account (No. 179-131).

For deferral account No. 179-70, Board Staff proposed additional wording for the accounting order. Union accepts those changes.

For deferral account No. 179-131, Board Staff requested that Union explain the first entry on the accounting order. The first entry captures the amount of optimization revenue refunded to customers in approved rates. The second entry captures the actual optimization to be refunded to ratepayers. The resulting balance in the account will be the variance between the actual optimization revenue to be refunded and the actual amount refunded in approved rates.

The two separate entries are required to ensure the effect of any volume-related variance is captured in the deferral account. If Union's sales service volumes are greater than forecast the amount refunded to customers will be higher than forecast, similarly, if sales service volumes are less than forecast the amount refunded to customers will be lower than forecast. Accounting for the actual volumes in the deferral account ensures there is no gain or loss resulting from the credit for upstream optimization included in rates.

CME

CME's submission dated December 31, 2012 stated that Union's DRO was complex and required a narrative to explain the drivers. CME's "specific comments on the DRO" were limited to Optimization Margin. Union's response to CME's comments is provided below.

APLP

APLP's submission dated January 3, 2013 urged "the Board to direct Union to consider appropriate rate mitigation measures" because APLP's total bill impact exceeds 31%. Union's response to APLP is included in the Rate Mitigation section below.

Complexity of DRO

Following the release of the Board's Decision and subsequent to the preparation of the DRO, Union convened a meeting with intervenors and Board Staff on December 5, 2012 to explain the change in revenue deficiency, the calculation of rates and the rate impacts, including the major drivers of the changes by rate class, based on the Board's Decision. Schedules were provided to intervenors and Board Staff in advance of the meeting to allow parties to review the information and prepare questions for Union's DRO panel. During the meeting Union explained the schedules and responded to questions from intervenors.

Subsequent to the December 5, 2012 meeting and Union's filing of the DRO on December 13, 2012, Union received telephone calls and/or emails from LPMA, Board Staff, CME and the

Association of Power Producers of Ontario ("APPrO") requesting further clarification. Union provided responses to all inquiries.

As noted above, LPMA and Board Staff support the determination of rates per the Board's Decision as filed by Union. APPrO did not make a submission.

CME stated that the DRO was complex and requested Union to provide 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 South respectively."

Union appreciates that the DRO is cumbersome. However, it is important to recognize that the 2013 DRO includes the same schedules used by Union in its pre-filed evidence (November 2011) and its evidence updates (March 2012 and July 2012). To the extent Union has provided additional schedules, these are intended to provide additional explanation of Union's 2013 rates and are a direct result of the Board's Decision. The new schedules (e.g. Rate Order, Working Papers, Schedule 11) present the rate changes from the Settlement Agreement to the Board's Decision by rate class.

Union believes that it responded to the questions posed in CME's submission through the December 5, 2012 meeting and a subsequent December 20, 2012 conference call. In response to CME's submission, the information is set out again below.

Rate Changes - DRO vs. Settlement Agreement

On page 3 of its December 31, 2012 letter CME submitted:

> "*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.*"

Union North Delivery Rates

Per the Board's Decision, Union has used a 50:50 blended approach of the 20-year declining trend and the 30-year average methodology to derive total Heating Degree Day estimates for

2013. Union has also increased 2013 customer attachments by 800 customers to reflect the customers forecasted to attach in Red Lake and increased 2013 contract customer demand forecast revenue. Accordingly, Union North forecasted delivery revenue has increased by $3.380 million, from $179.100 million in the Settlement Agreement to $182.480 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 1 to 6, columns a, b and c) for the rate class details.

In accordance with the "Report of the Board on the Cost of Capital for Ontario Regulated Utilities", the return on equity has been calculated using September 2012 actual and forecast bond yields. The updated ROE for 2013 is 8.93%. Per the Board's Decision, Union has reflected an equity thickness of 36% and storage assets have been allocated to the regulated business using the updated storage allocation factors provided in Exhibits J8.3, J8.4 and J8.5. Accordingly, the Union North delivery-related revenue requirement has decreased by $4.847 million, from $222.866 million in the Settlement Agreement to $218.019 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 1 to 6, columns d, e and f) for the rate class details. The Union North delivery-related revenue requirement changes from the Settlement Agreement to the DRO can also be found at Rate Order, Working Papers, Schedule 6, page 2, columns t through x).

The increase in forecasted Union North delivery revenue and the decrease in Union North delivery-related revenue requirement reduce Union's proposed delivery rate increases by $8.227 million in the DRO as compared to the Settlement Agreement.

In its Decision and Order, the Board found that Union's use of S&T margin as a rate design tool to manage rate impacts, rate continuity and revenue-to-cost ratios is not appropriate, and that S&T margin should be allocated to rate classes on the basis of sound regulatory principles. Per the Board's Decision, the S&T transactional margin allocated to Union North delivery rates has decreased by $8.695 million, from $13.135 million in the Settlement Agreement to $4.440 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 1 to 6, columns g) through l) for the rate class details. Please see Rate Order, Working Papers, Schedules 41 and 42 for the allocation of S&T margin to Union North rate classes.

In total, the changes in forecasted revenue, revenue requirement and S&T transactional margin to reflect the Board's Decision have increased the proposed Union North delivery rate increase by $0.469 million, from $30.630 million in the Settlement Agreement to $31.099 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 1 to 6, columns m, n and o) for the rate class details. The Union North delivery rate increase of $31.099 million can also be found at Rate Order, Working Papers, Schedule 10, line 1.

Union South Delivery and Storage Rates

Per the Board's Decision, Union has used a 50:50 blended approach of the 20-year declining trend and the 30-year average methodology to derive total Heating Degree Day estimates for 2013. Union has also increased 2013 contract customer demand forecast revenue. Accordingly, Union South forecasted delivery and storage revenue has increased by $5.417 million, from $510.391 million in the Settlement Agreement to $515.808 million in the DRO. Please see Rate

Order, Working Papers, Schedule 11, page 1, lines 7 to 16, columns a, b and c) for the rate class details.

As described above, Union has reflected an updated ROE for 2013 of 8.93% and the Board's Decision on equity thickness and updated storage allocation factors. Accordingly, the Union South delivery and storage-related revenue requirement has decreased by $12.000 million, from $546.323 million in the Settlement Agreement to $534.324 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 7 to 16, columns d, e and f) for the rate class details. The Union South delivery and storage-related revenue requirement changes from the Settlement Agreement to the DRO can also be found at Rate Order, Working Papers, Schedule 6, page 1.

The increase in forecasted Union South delivery and storage revenue and the decrease in Union South delivery and storage-related revenue requirement reduce Union's proposed delivery and storage rate increases in Union South by $17.417 million in the DRO as compared to the Settlement Agreement.

Per the Board's Decision on S&T margin described above, the S&T transactional margin allocated to Union South delivery and storage rates has decreased by $1.046 million, from $10.778 million in the Settlement Agreement to $9.732 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 7 to 16, columns g) through l) for the rate class details. Please see Rate Order, Working Papers, Schedules 41 and 42 for the allocation of S&T margin to Union South rate classes.

In total, the changes in forecasted revenue, revenue requirement and S&T transactional margin to reflect the Board's Decision have decreased the proposed Union South delivery and storage rate increase by $16.371 million, from $25.154 million in the Settlement Agreement to $8.783 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, lines 7 to 16, columns m, n and o) for the rate class details. The Union South delivery and storage rate increase of $8.783 million can also be found at Rate Order, Working Papers, Schedule 10, line 2.

To summarize, proposed Union North delivery and Union South delivery and storage rate increases have decreased by $15.902 million, from $55.784 million in the Settlement Agreement to $39.882 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 1, line 17, columns m, n and o).

Union North Transportation and Storage Rates

Per the Board's Decision to use a 50:50 blended approach to derive total Heating Degree Day estimates for 2013 and increase the 2013 customer attachments by 800 customers to reflect the customers forecasted to attach in Red Lake, Union North forecasted transportation and storage revenue has increased by $2.745 million, from $101.882 million in the Settlement Agreement to $104.628 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 1 to 6, columns a, b and c) for the rate class details.

The Union North transportation and storage-related revenue requirement has increased by $38.273 million, from $104.577 million in the Settlement Agreement to $142.850 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 1 to 6, columns d, e and f) for the rate class details.

As described in Union's December 13, 2012 DRO cover letter, per the Settlement Agreement, upstream transportation costs in Union North delivery, transportation and storage rates reflected Union's 2013 Gas Supply Plan and upstream transportation tolls as approved in Union's January 2011 QRAM. Union North delivery, transportation and storage rates recovered upstream transportation costs of $88.622 million.

In the DRO, upstream transportation costs in Union North delivery, transportation and storage rates reflect current upstream tolls (as of October 1, 2012) associated with the upstream transportation contracts per Union's 2013 Gas Supply Plan. Union North delivery, transportation and storage rates will recover upstream transportation costs of $126.328 million.

Compared to upstream transportation costs of $133.193 million in Union's current approved Union North delivery, transportation and storage rates (per April 2011 QRAM), the upstream transportation costs in Union's proposed Union North delivery, transportation and storage rates in the DRO of $126.328 million represent a decrease of $6.865 million.

Per the Board's Decision, 90% of forecasted gas supply optimization margin has been included in the gas supply transport revenue requirement. Accordingly, the amount of gas supply optimization margin allocated to Union North transportation and storage rates has increased by $5.856 million, from zero in the Settlement Agreement to $5.856 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 1 to 6, columns g, h and i). Please see Rate Order, Working Papers, Schedule 44 for the allocation of gas supply optimization margin to Union North rate classes.

In total, the changes in forecasted revenue, revenue requirement and gas supply optimization margin to reflect the Board's Decision have increased the proposed Union North transportation and storage rate increase by $29.678 million, from $2.705 million in the Settlement Agreement to $32.383 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 1 to 6, columns m, n and o) for the rate class details. The Union North transportation and storage rate increase of $32.383 million can also be found at Rate Order, Working Papers, Schedule 10, lines 3 and 4 ($38.239 million less $5.856 million).

<u>Ex-Franchise Rates</u>

Per the Board's Decision to use a 50:50 blended approach to derive total Heating Degree Day estimates for 2013 and increase the 2013 forecast to reflect FT-RAM activity, forecasted ex-franchise transportation and exchange revenue has increased by $4.694 million, from $202.982 million in the Settlement Agreement to $207.676 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 8 to 12, columns a, b and c) for the rate class details.

As described above, Union has reflected an updated ROE for 2013 of 8.93% and the Board's Decision on equity thickness and updated storage allocation factors. Accordingly, the ex-franchise transportation and exchange revenue requirement has decreased by $5.878 million, from $180.349 million in the Settlement Agreement to $174.471 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 8 to 12, columns d, e and f) for the rate class details.

In total, the changes in forecasted revenue and revenue requirement to reflect the Board's Decision have resulted in a rate decrease for ex-franchise rates of $5.448 million, from a rate increase of $1.467 million in the Settlement Agreement to a rate decrease of $3.981 million in the DRO. Please see Rate Order, Working Papers, Schedule 11, page 2, lines 8 to 12, columns m, n and o) for the rate class details. The ex-franchise rate decrease of $3.981 million can also be found at Rate Order, Working Papers, Schedule 10, line 6.

Gas Supply Administration Charge

Per the Board's Decision, Union has reduced the gas supply administration charge from 0.3138 cents/m^3 to 0.1933 cents/m^3 (or 0.1205 cents/m^3) to reflect the gas supply administration charge sufficiency of $4.260 million. For example, please see Rate Order, Appendix A, page 6, line 1, column b) for Union South and Rate Order, Appendix A, page 1, line 21, column b) for Rate 01 in Union North. The gas supply administration charge decrease of $4.260 million can also be found at Rate Order, Working Papers, Schedule 10, line 7.

Union South Gas Supply Transportation Rates

Per the Board's Decision, 90% of forecasted gas supply optimization margin has been included in the gas supply transport revenue requirement. Accordingly, the amount of gas supply optimization margin allocated to Union South gas supply transportation rates has increased by $7.571 million, from zero in the Settlement Agreement to $7.571 million in the DRO. As a result, the Union South gas supply transportation rate has decreased from 4.6821 cents/m^3 to 4.3997 cents/m^3 (or 0.2824 cents/m^3). Please see Rate Order, Appendix A, page 6, line 3. The Union South gas supply transportation rate decrease of $7.571 million can also be found at Rate Order, Working Papers, Schedule 10, line 8. Please see Rate Order, Working Papers, Schedule 44 for the allocation of gas supply optimization margin to Union South rate classes.

Gas Supply Commodity Sufficiency

The gas supply commodity sufficiency of $44.414 million found at Rate Order, Working Papers, Schedule 10, line 10 reflects the timing difference between gas supply commodity rates in forecasted revenue as compared to the gas supply commodity costs in the revenue requirement. Forecasted revenue, including gas supply commodity revenue, is based on January 2011 QRAM rates, whereas per the Settlement Agreement, the gas supply commodity costs in the revenue requirement are based on July 2012 QRAM rates.

In the DRO, Union is not proposing any change to gas supply commodity rates. The gas supply commodity sufficiency of $44.414 million has already been refunded to sales service customers through the QRAM from January 2011 to July 2012. Union will continue to set gas supply commodity rates as part of the QRAM.

Optimization

In its submission, CME questions whether Union has interpreted the Board's Decision with respect to upstream optimization revenues correctly. In the DRO, Union classified all forecasted upstream optimization net margins, including margins derived from exchanges (base exchanges and FT-RAM) as offsets to the gas supply costs.   CME interprets the Board's Decision such that only optimization net margins derived from FT-RAM related exchanges should be treated as gas cost reductions. In CME's view, all other optimization revenues should be treated differently and for the benefit of all in-franchise ratepayers because 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."

Union disagrees with CME. The premise of CME's view is contrary to the Board's Decision and the evidence at the hearing that there is no distinction between base exchanges and FT-RAM related exchanges other than the use of the FT-RAM program in the latter case. At p. 25 of the Decision (not referred to in CME's letter), the Board indicated that "[e]xchange revenue is comprised of activity using Union's upstream transportation capacity to provide exchange services to third parties. It also includes net revenue generated from pipe releases or revenue from [FT-RAM] program."

Later, p. 39 of the Decision provides:

> *"Consistent with the long-standing principle that a gas utility should not profit from the procurement of gas supply for its in-franchise customers, and to eliminate the creation of inappropriate incentives during the test year, the Board finds that the optimization activities, as defined below, are to be considered part of gas supply, not part of transactional services.*
>
> *The Board reiterates that gas supply costs refer to both the upstream gas cost, including fuel gas, and the cost (rate multiplied by contract volume) of upstream transportation that is required to deliver gas supply to Union's in-franchise customers in the North and South Delivery Areas.*
>
> *Consistent with the description provided by Union, the Board will define optimization as <u>any market-based opportunity to extract value from the upstream supply portfolio held by Union to serve in-franchise bundled customer</u>s, <u>including, but not limited to, all FT-RAM activities and exchanges</u>."* [Emphasis added]

Exchange revenues are created by Union optimizing its upstream transportation contracts and its integrated assets. The upstream transportation contracts held by Union are to provide services to in-franchise customers, including all sales service customers and bundled direct purchase customers in Union North. As noted above in the Board's Decision, optimization revenue is defined as any opportunity or transaction that uses Union's in-franchise upstream portfolio. Since all upstream transportation contracts are held for in-franchise customers, the optimization revenues generated from those assets are to be included as part of the gas supply plan.

CME states that "base exchange" revenues and "FT-RAM exchange" revenues should be treated differently.

On the contrary, and as noted by Board Staff in its submission, the Decision states at p. 117:

> *"As ordered previously, the amount built into rates related to gas supply optimization is 90% of Union's 2013 forecast of base exchanges and 90% of half of Union's FT-RAM 2013 forecast."*

It is clear that the Board required Union to include all exchange revenues, both base exchange revenues and FT-RAM revenues as gas cost reductions.

Rate Mitigation

As stated in the October 18, 2012 Report of the Board titled Renewed Regulatory Framework for Electricity Distributors: A Performance-Based Approach Board's at Section 2.4:

> "Rate mitigation has been a policy of the Board since 2000. At that time, the Board established a requirement that distributors *consider* mitigation where total bill increases for any customer class exceed 10%. Since only consideration and not implementation of mitigation is required, this percentage is referred to as a "soft" threshold. The most recent articulation of the Board's mitigation policy confirmed the continuation of the "soft" 10% threshold for the filing of mitigation plans and provides guidance to distributors on preparing those plans. In its mitigation plan a distributor may propose any, or no, mitigation mechanism as may be suitable in a particular circumstance."

As filed at Working Papers Schedule 17, no rate class has a delivery bill impact that is greater than 10% of total bill.

Board Staff

Board Staff agreed in their submission, stating that:

> *"Board Staff notes that there are no rate classes where the bill impact is greater than 10% on the total bill. As such, Board Staff submits that no rate mitigation is required."*

CME

CME stated the Board should "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".

Union disagrees with CME. In Union's view, it is inappropriate to phase-in the rate decreases and rate increases in the contract rate classes over a period of two or more years, as suggested by CME.

In its Decision, the Board set Union's 2013 forecasted revenue and approved Union's 2013 cost allocation study. Union's proposed rates in the Draft Rate Order reflect the implementation of the Board's Decision. CME's submission suggests, where, as an example Rate T2 rates are decreasing by 22.5% and Rate M4 rates are increasing by 15.5%, that Rate T2 customers should not receive the rate decrease resulting from the Board's Decision, but rather should cross-subsidize Rate M4 customers by paying a portion of the approved costs allocated to Rate M4, for a period of two years or more. In Union's submission, CME's suggestion is not consistent with the Board's Decision and should be rejected.

Given that the delivery bill impacts on the total bill do not exceed 10% for any rate class, rate mitigation is not required.

APLP

APLP's calculation of the total bill impact is incorrect. APLP calculated the 31% bill impact by comparing its Union Gas delivery charges only and did not take into account the third party gas supply commodity and upstream transportation charges that form the total bill.

As seen at Working Papers, Schedule 17, the delivery bill impact of the DRO on the total bill (including gas supply commodity and upstream transportation costs), as compared to Union's January 2013 QRAM rates for a small Rate 100 customer is 1.0%, and for a large Rate 100 customer is 0.9%

Based on this analysis, rate mitigation is not required. If Union were to implement rate mitigation measures to reduce the impacts to Rate 100 customer, then delivery rates for other customers in Union North would need to be increased to ensure Union's approved costs are recovered.

No other intervenor made a submission, including the Industrial Gas Users Association and APPrO.

Notices

CME states that the Union's draft Notices do not help contract customers "understand the causes for the rate changes that the Board has approved". Union's current rate Notices, both for general service and contract customers, were developed with Board Staff's Communications group in 2008. The Notices were developed to create a standardized Notice that customers would recognize as a communication tool informing them that rates are changing.

Union will address the need for more detailed explanations with customers as follows:

- For general service customers, Union will provide a bill insert that will explain the changes in distribution rates for 2013. This insert will be included with the first customer invoice for 2013 rates.

- For contract rate customers, Union is not aware of customer concerns related to its past communication of rate changes. Union has communicated the 2013 rate case proposals at customer meetings throughout 2012. In addition, consistent with past practices, Union will explain Board-approved changes in rates via email to each contract rate customer. The e-mail communications will be more detailed than the draft rate Notices, and will provide an explanation of the major drivers of change and rate impacts. Also, consistent with past practices, in response to customer requests, Union Account Managers will meet with large contract customers on a one to one basis to discuss Union's 2013 rates Decision and specific rate impacts.

No other party made a submission on Union's Notices.

In Union's view, the draft Notices are intended to inform customers that rates are changing and the text should not be altered. The Notices are clear and do not confuse the customer. Union's other initiatives including the bill insert, emails and face-to-face meetings address CME's concern about a customer's lack of understanding.

<u>Implementation</u>

The rate changes proposed in the Draft Rate Order will be effective January 1, 2013.

Union proposes to implement new rates on the first billing cycle on or after February 1, 2013. Union proposes that any variances between the rates charged to customers during the period January 1 to January 31, 2013 and the rates included in the Draft Rate Order shall form part of the price adjustment to be recovered from each rate class.

Union requests the Board's Decision on the Draft Rate Order by Friday, January 18, 2013 in order to implement rates February 1, 2013, effective January 1, 2013.

If you have any questions with respect to this submission, please contact me at 519-436-5476.

Yours truly,

[original signed by]

Chris Ripley
Manager, Regulatory Applications

cc: Crawford Smith, Torys
EB-2011-0210 Intervenors