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By electronic filing

June 24, 2014

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

Dear Ms. Walli,

Union Gas Limited
2014 Rates Application
Board File No.: EB-2013-0365
Our File No.: 339583-000169

Please find enclosed the Written Argument of Canadian Manufacturers & Exporters ("CME") in the above-noted proceeding.

Yours very truly,

A handwritten signature in black ink, appearing to read 'P. Thompson', with a long horizontal flourish extending to the right.

Peter C.P. Thompson, Q.C.

PCT\slc
enclosure

c. Chris Ripley (Union Gas)
Paul Clipsham and Ian Shaw (CME)
Vince DeRose

OTT01: 6399038: v1

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 Union Gas Limited pursuant to section 36(1) of the *Ontario Energy Board Act, 1998*, for an order or orders approving or fixing just and reasonable rates and other charges for the sale, distribution, transmission and storage of gas as of January 1, 2014.

**ARGUMENT OF
CANADIAN MANUFACTURERS & EXPORTERS (“CME”)**

June 24, 2014

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I. INTRODUCTION

1. There are two issues which remain outstanding in this case. The first pertains to cost allocation. The second pertains to rate-related contract terms which Union Gas Limited (“Union”) has demanded of certain greenhouse growers without obtaining prior Board approval for those terms.

II. COST ALLOCATION

A. Board Directives

2. The proponents for cost allocation changes with respect to the Parkway and Kirkwall Station costs are criticized by Union and others for raising these issues in Union’s 2014 Rates proceeding. Union and others argue that cost allocation issues of this nature should be deferred to Union’s 2019 Rates case when its rates are to be rebased.
3. These arguments lack merit because, in prior proceedings, the Board specifically directed that Parkway Station and Kirkwall Station cost allocations be reviewed in this particular proceeding. The “Station” cost allocation issues in this 2014 proceeding stem from Board directions in three prior decisions.
4. The first of these directives was contained in a Board Decision in EB-2010-0296 dated November 30, 2010. In that case, the Board approved modifications to Union’s M12 rate schedule to accommodate bi-directional M12X service and to its C1 rate schedule to accommodate transportation service from Kirkwall to Dawn. The costs of the facility modification at the Kirkwall Station to support such services were about \$4.7M. In that proceeding, Union directly assigned those costs to the new services and recovered them in a demand charge. The Board approved Union’s proposed approach subject to a directive that the cost allocations be reviewed in Union’s 2013 Rebasing case as follows.

“The Board directs Union to review the rate-making methodology of the proposed services as part of its rebasing in 2013. The Board agrees with the submission of Board staff that Union’s proposal to allocate all of the costs related to the facility modifications to C1 Kirkwall to Dawn customers raises concerns regarding Union’s compliance with cost allocation principles. The Board agrees with Board staff that it is reasonable to review cost allocation and rate design for the proposed transportation services at the time of rebasing, given the relatively small annual revenue requirement related to the facilities and the

uncertainties regarding how shippers plan to use the proposed services.”

5. The second of these directives was contained in a Board Decision and Order in EB-2011-0257 dated September 13, 2011. In that case, Union sought approval of modifications to its C1 and M12 rate schedules to accommodate the provision of transportation service from Kirkwall to Parkway. The Board did not conduct any detailed analysis of the appropriateness of the cost allocation and rate design methods which Union applied in that proceeding. Rather, as it did in the prior case, the Board directed Union to review its cost allocation and rate design proposals in its rebasing case for the 2013 year as follows:

“The Board directs Union to review the rate-making methodology of the proposed services as part of its rebasing in 2013. The Board agrees with Board staff that it is reasonable to review cost allocation and rate design for the proposed transportation services at the time of rebasing.”

6. Union’s response to these directives in its 2013 rebasing case was incomplete. Moreover, in that 2013 rebasing case, John Rosenkranz provided expert evidence on behalf of the Federal of Rental-housing Providers of Ontario (“FRPO”), the Corporation of the City of Kitchener (“Kitchener”), the Consumers Council of Canada (“CCC”), and CME. That evidence focused on the separation of Parkway Station costs from overall Dawn-Trafalgar easterly transportation costs. While the Board did not approve Mr. Rosenkranz’s recommendations in that case, it did issue a directive that Parkway Station costs be revisited in Union’s 2014 rates proceeding as follows:

“The Board will revisit this issue as part of Union’s 2014 rates proceeding, after the Board receives Union’s report on the outcome of the Parkway Obligation Working Group.”¹

7. Moreover, with respect to Kirkwall Station costs, the Board accepted the submissions made by London Property Management Association (“LPMA”) to the effect that considerable change had taken place with respect to the gas flows around the Parkway Station since Union last reviewed the cost allocation and rate design for services offered on the Dawn-Trafalgar system in 1995 and that the Board last approved Union’s 1997

¹ EB-2011-0210 Decision and Order dated October 24, 2012, p.73.

rate case which was E.B.R.O. 493/494. In response to LPMA's submission, the Board stated as follows:

“The Board agrees with the submissions of LPMA. The use of the Kirkwall Station has changed substantially over the years and there is a clear need to review the allocation of Kirkwall Station costs. The Board directs Union to undertake a review of the allocation of Kirkwall metering costs as part of its updated cost allocation study which the Board has directed Union, later in this Decision, to file in its 2014 rates filing.”²

8. As a consequence of these directives, it is submitted that the Board clearly intended that matters pertaining to the allocation of Parkway and Kirkwall Station costs be considered in this proceeding and determined before Union's rebasing proceeding in 2019. These directives cannot reasonably be interpreted otherwise. The arguments made by Union and others to the effect that issues pertaining to the appropriateness of Union's allocation of “Station” costs should be deferred to Union's 2019 rebasing case are incompatible with these directives. Such arguments should be rejected.
9. The fact that the alleged misallocations of costs are “modest” as Union argues, does not detract from the directives calling for these items to be addressed in this proceeding. Contrary to Union's Argument, the sponsors of Mr. Rosenkranz's evidence are not prematurely seeking modest changes in search for a “better mousetrap”. Rather, they are seeking to complete the cost allocation agenda in a manner which appropriately responds to the prior Board directives.

B. The Evidence of John Rosenkranz

10. As a consequence of these directives, FRPO, the Ontario Greenhouse Vegetable Growers (“OGVG”), Kitchener, CME retained Mr. Rosenkranz to provide his analysis of Union's response to matters pertaining to the allocation of “station” costs. Parkway Station, like Dawn Station, has both Metering and Regulating (“M&R”) and compression facilities. Kirkwall has only M&R facilities. Mr. Rosenkranz's analysis responds to both the Parkway Station and Kirkwall Station directives and adheres to the objective implicit therein of having these “Station” cost allocation issues resolved before rebasing in 2019.

² EB-2011-0210 Decision and Order dated October 24, 2012, p.74.

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11. Mr. Rosenkranz's analysis logically encompasses a consideration of Union's approach to the allocation of costs at the Dawn Station which, like Parkway, includes M&R facilities as well as compression facilities. It encompasses a consideration of the Kirkwall Station, which has no compression facilities. The Lobo and Bright Stations on the Dawn-Parkway transmission system house compression facilities only. We submit that the method to be used to allocate M&R costs at the Dawn, Kirkwall and Parkway Stations should be consistent. Similarly, the method used to allocate compression costs at Dawn, Lobo, Bright and Parkway should also be consistent. Accordingly, while Dawn Station costs were not specifically identified by the Board as being a subject for review in this proceeding, we submit that it would be reasonable to correct for inappropriate "Station" cost allocations at Dawn at the same time that corrections are made to misallocation of Station costs at Kirkwall and Parkway.
 12. As a result of his analysis, Mr. Rosenkranz concludes that Union's in-franchise customers are being over-allocated costs associated with the Parkway, Kirkwall and Dawn Stations in an amount of about \$1.4M per year, or about \$7.0M over the course of the 5 year IRM. This amount, while modest, is nevertheless material. These misallocations should be corrected now rather than being allowed to prevail until 2019. Union's M12 and C1 customers should not be subsidized for a further four years by in-franchise ratepayers.
 13. There is nothing in the Settlement Agreement which precludes the Board from correcting these cost misallocations now. In fact, in the Settlement Agreement, Union expressly accepted that any cost allocation changes to Kirkwall metering are to be implemented on January 1, 2015. The settlement is silent with respect to other inappropriate cost allocations pertaining to Dawn-Parkway system "Station" costs with the result that the Board can and should correct all misallocation of such costs effective January 1, 2015.
 14. Mr. Rosenkranz's evidence shows that certain aspects of Union's cost allocation methodology are incompatible with the principle of cost causality. In particular, Union's use of a distance-based factor to allocate costs that are not related to distance under-allocates costs to new short-haul transportation services such as the M12 Kirkwall to Parkway service. This distorts the price signals that drive future investments in Union's transmission facilities.

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15. To be clear, Mr. Rosenkranz is not recommending that the Board reject the distance-based allocation methodology that Union uses for Dawn-Parkway system costs. What he is suggesting is that this allocation methodology should only be applied where:
- (a) It is not possible to assign or allocate costs to the customer classes that use specific facilities; and
 - (b) The costs being allocated are related to the distance that the natural gas is transported on the Dawn-Parkway system.

C. Measuring and Regulating (“M&R”) Costs

16. It is common ground with Union that the distance which gas flows on its system has nothing to do with the incurrence of M&R facilities costs at the Dawn, Kirkwall and Parkway Stations. Union operates M&R facilities at Kirkwall and Parkway that are primarily, if not exclusively, used to provide services to ex-franchise Rate M12 and Rate C1 customers. The Kirkwall meter modifications approved in EB-2010-0296 are one example and the Parkway Station M&R facilities at the Lisgar Delivery Point, which are only used to deliver gas to Enbridge Gas Distribution Inc. (“EGD”), are another.
17. We agree that the Kirkwall and Parkway M&R costs should be allocated on the basis of the manner in which those facilities are used on a “design day” as Union argues. The “design day” is the peak requirement under “design” operating conditions and Mr. Rosenkranz recommends that the peak day allocation factor should be used to allocate M&R costs at Kirkwall, Parkway and Dawn, being all of the Dawn-Parkway system stations with M&R facilities.
18. At Kirkwall and Parkway, the M&R facilities are primarily used to receive and deliver gas between Union and its M12 customers such as TransCanada PipeLines Limited (“TCPL”) and EGD. Put another way, a greater portion of the design day of these facilities is used to provide M12 services when compared with other parts of the integrated Dawn-Parkway system. The mix of customers using the M&R facilities at Kirkwall and Parkway on either the peak day or the design day is materially different from the mix of customers using the Dawn-Parkway mainline. Mr. Rosenkranz recommends and we submit that Union’s cost study should reflect this reality. The costs

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- of these facilities should be borne by the customers that use them instead of being allocated to all users of the Dawn-Parkway system.
19. In his evidence, at page 7, Mr. Rosenkranz tried to illustrate this fact by pointing out that under the current cost allocation methodology applied by Union, an in-franchise customer in Union's South pays a portion of the costs for M&R facilities that are used to deliver gas from the Dawn-Parkway system to TCPL for ex-franchise shippers, but ex-franchise customers do not pay any portion of the M&R facilities that are used to deliver gas from the Dawn-Parkway system to the in-franchise customers since these M&R facilities are classified as Other Transmission or Distribution, both of which are allocated solely to in-franchise customers. The distance-based allocation factor makes sense for a pipeline and compression facilities that are used by all in-franchise and ex-franchise customers that ship gas on the integrated Dawn-Parkway transmission system. However, the use of this factor does not make sense for facilities that are used more heavily by specific classes of customers and where the use of these facilities can be identified for cost assignment or allocation purposes.
 20. The "entire integrated system" does not cause the cost of M&R facilities at Kirkwall and Parkway to be incurred. Rather, it is the demands of customers served primarily under the auspices of the ex-franchise transportation rates which flow through those meters which give rise to those costs. The M&R costs are caused by the customer class demands which are expected to flow through the meters and should be allocated accordingly. It is the expected demands which cause the costs to be incurred, regardless of whether the gas is flowing in one or two directions. The distance of travel has no causal connection with the M&R costs being allocated. When the M&R facilities are not used to serve in-franchise peak day demands, then there should be no allocation of M&R costs to in-franchise ratepayers.
 21. The distance-based factor that Union currently applies to Kirkwall and Parkway M&R costs is incompatible with M&R cost causality. Union's approach does not best reflect M&R cost causality as Union argues. It does not reflect M&R cost causality at all. The fact that Union's approach is incompatible with M&R cost causality should prompt the Board to direct Union to correct the misallocations regardless of its prior approval of Union's approach in Union's 1997 rate case.

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22. Union already allocates Dawn Station M&R costs that are included in the Dawn Station cost category to the customer classes that use these facilities based on peak day demands without a distance adjustment. The same demand-based methodology should be used for Kirkwall and Parkway Stations M&R costs.
 23. In summary, Kirkwall and Parkway M&R costs that can be directly assigned to customer classes should be directly assigned and Kirkwall and Parkway M&R costs that cannot be directly assigned should be allocated on the basis of peak day demands. To implement these recommendations, Union will be required to develop separate cost allocation factors for Kirkwall Station and Parkway Station based on the peak day demands to deliver and/or receive gas at that meter just as Union currently does for Dawn Station costs. Union's response to Board Staff Interrogatory Exhibit B1.3 illustrates how the cost allocation factor could be calculated for Kirkwall.
 24. In his review of Union's allocation of Dawn-Parkway system costs, Mr. Rosenkranz found that Union functionalizes some of the costs at the Dawn Station M&R assets that are used for Dawn-Parkway transmission service as "Dawn Station" costs and functionalizes the rest of these costs as "Dawn-Trafalgar Easterly" costs. Union also does this with Dawn Station compression costs. Union does not and cannot explain how or why it divides Dawn M&R costs and Dawn compression costs between these two "buckets" which are then allocated to customer classes using different allocation factors. Accordingly, there is no cost causality rationale for these allocations of Dawn Station costs.
 25. We submit that to provide an allocation of M&R costs for each of the three Stations on the Dawn-Parkway transmission systems with such facilities, Union should be directed to functionalize all Dawn M&R costs that are related to the Dawn-Parkway system to the Dawn Station category and to allocate all of these costs using the demand-based Dawn ("DAWNCOMP") cost allocation factor.

D. Compression Costs

26. Unlike M&R costs, the costs of compression are directly linked to the distance which gas flows. Accordingly, allocating compression costs on the basis of a distance-based allocation factor is appropriate.

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27. Union uses an appropriate allocation factor to allocate all of the compression costs at the Lobo and Bright Stations. However, the bulk of the compression costs that Union incurs at Dawn are allocated under the auspices of a peak day demand allocation factor rather a distance-based allocation factor. This should be corrected. Dawn compression costs that are used for the operation of the Dawn-Parkway system should be functionalized as Dawn-Trafalgar Easterly costs and allocated using the Distance-weighted Demand Allocator (“DTTRANS”) just as Union currently allocates compressor costs at the Lobo and Bright compression stations.
28. The Board’s decision to revisit the allocation of Parkway Station costs in this proceeding applied to both M&R costs and compression costs since both types of costs were considered in EB-2011-0210 case. The Board has all the information it needs to act on misallocations pertaining to the Kirkwall, Parkway and Dawn M&R costs and the corrections to the functionalization of Dawn M&R and compression costs. However, having regard to the Board’s recent Decision approving further facilities at Parkway, cost allocation issues pertaining to Parkway compressor facilities and their implications for rate classes will need further investigation. We agree that this further investigation of matters related to the compression costs at the Parkway Station should take place in Union’s 2019 rebasing proceeding.

E. Summary

29. In summary, we urge the Board to direct Union to:
- (a) Correct the misallocation of M&R costs at the Kirkwall, Parkway and Dawn Stations and to bring forward those corrections in its 2015 rate case; and to
 - (b) Correct the misallocation of compression costs at the Dawn Station and to bring forward those corrections in its 2015 rate case.

III. UNION’S LEAMINGTON LINE PROJECT CONTRACTING PRACTICES

30. The facts pertaining to Union’s Leamington Line contracting practices are summarized in the submissions of Union and others. In our submission, the generic issue which these facts raise for other customers served under the auspices of contract rates is whether

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- contract provisions requiring customers to pay Union for a minimum annual volume of distribution services are enforceable without prior Board approval.
31. A determination of this generic issue does not turn on a question of misrepresentation as Union suggests in its Argument. Rather, it turns on whether the minimum annual payment provisions of each contract constitute a “rate” and, if so, whether Union has obtained Board approval for those contractual provisions.
 32. During the course of their testimony, Union’s witnesses readily conceded that the contractual provisions in issue in Union’s contracts with the greenhouse growers served off the Leamington Line are, in substance, minimum annual revenue provisions. In argument, Union effectively concedes this point by characterizing these contract provisions as a “contractual revenue commitment”. These contractual provisions effectively require each customer to pay a fixed annual charge for gas distribution services in an amount equivalent to Union’s calculation of each particular customer’s proportionate share of the costs of constructing the pipeline.
 33. On the authority of the Board’s Decision with Reasons in EB-2012-0396 dated February 17, 2013, the minimum annual payment provisions of these contracts are a “rate”. Under the *Ontario Energy Board Act, 1998* (the “Act”), a “rate” must be approved by the Board before it can be enforced by Union. Absent a prior Board approval, the minimum annual payment provisions in each of the contracts between Union and the Leamington Line greenhouse growers are unenforceable.
 34. The evidence indicates that the Board has not yet approved the minimum annual payment provisions of these contracts. The forecasts upon which Union based its Application for Leave to Construct (“LTC”) of the Leamington Line, reflected Union’s assumption that each of the greenhouse growers, who expressed interest in the proposed expansion of the distribution system, would be a source of revenue for 10 years. However, the Board’s LTC approval did not authorize Union to convert its 10 year forecast of revenue into a minimum annual delivery services charge for each customer so as to cover Union’s calculation of each customer’s proportional responsibility for the costs of the line. Union was free to ask customers to sign contracts to take service for periods longer than a year but the price for the distribution services to be provided by Union under such contracts has to be in accordance with Board approved rates.

35. As far as we are aware, there is nothing in the Leamington Line Expansion Open Season Notice found at Exhibit A, Tab 6, Appendix A indicating that customers would be required to sign multi-year contracts containing minimum annual payment provisions requiring each of them to pay Union's calculation of their proportionate responsibility for the capital cost of the line. The relevant provision of the Open Season Notice was as follows:

"1. Service Description and Details:

Term:

As this expansion project requires a significant capital investment and is being constructed during a period of changing gas supply dynamics, the term of these agreements is to be a minimum of one year contractual commitments and or upfront payment for capacity. The facilities, rates and services included in this binding Expression of Interest will be subject to OEB approval." (emphasis added)

This language gives no indication of a requirement for a minimum annual payment and, in any event, clearly represents that the rates and services will be subject to OEB approval.

36. There is nothing in the Board's Decision in EB-2012-0431 dated March 28, 2013, granting Union leave to construct the Leamington Line which approves the minimum annual payment provisions of the contracts Union subsequently entered into with the greenhouse growers taking service off that line.
37. Based on the foregoing, we respectfully submit that the minimum annual payment provisions in Union's contracts with the Leamington Line greenhouse growers are unenforceable. The remaining provisions in those contracts, including those pertaining to the duration of the contracts, remain valid. We urge the Board to make findings to that effect in this proceeding.
38. If the Board makes such findings, then Union will have two options by way of a response. Union can, if it wishes, apply to the Board in a subsequent proceeding for orders approving each of the customer-specific minimum annual payment provisions in its contracts with the Leamington Line greenhouse growers. If Union seeks such relief, then the growers and all other interested parties will be allowed an opportunity to make submissions as to whether the minimum annual payment provisions of each contract are

unduly discriminatory fixed charges which differ from the fixed charges other customers served under the auspices of Union's Rates M4 and M5A are required to pay.

39. On the other hand, if Union refrains from seeking Board approval of the minimum annual provisions of the contract, then each Leamington Line greenhouse grower will be obliged to pay for the gas distribution services it receives from Union. Until such time as Union obtains Board approval for the minimum annual payment provisions of the contracts, each greenhouse grower will pay for the distribution services it uses and no more.

IV. COSTS

40. CME requests that it be awarded 100% of its reasonably incurred costs in connection with this matter.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 24th day of June, 2014.



Peter C.P. Thompson, Q.C.
Vincent J. DeRose
Counsel for CME