Ontario Energy Board
Commission de l'Énergie de l'Ontario

VT INCEPIT FIDELIS SIC PERMANET
Ontario

RP-2002-0130

IN THE MATTER OF AN APPLICATION BY

UNION GAS LIMITED

FOR

YEAR 2003 RATES

DECISION WITH REASONS

2003 MAY 08

RP-2002-0130
EB-2002-0363

IN THE MATTER OF the *Ontario Energy Board Act*, 1998, S.O. 1998, c.15, Sched. B; 2

AND IN THE MATTER OF an Application by Union Gas Limited for an order or orders approving or fixing just and reasonable rates and other charges for the sale, distribution, transmission, and storage of gas for the period commencing January 1, 2003; 3

AND IN THE MATTER OF the customer review process and other mechanisms approved by the Ontario Energy Board in its decision in RP-1999-0017. 4

BEFORE: 5

Paul B. Sommerville 6
Presiding Member

Fred Peters 7
Member

8

<u>DECISION WITH REASONS</u>

May 8, 2003 9

TABLE OF CONTENTS 10

APPENDICES 12

DECISION WITH REASONS

1 THE APPLICATION AND THE PROCEEDING 14

1.1 The Application and Background 15

Union Gas Limited ("Union") filed an application dated May 27, 2002 (the "Application"), with the Ontario Energy Board (the "Board") pursuant to section 36 of the *Ontario Energy Board Act,* 1998, S.O. 1998, c. 15, Sched. B (the "Act"), for an order or orders approving or fixing just and reasonable rates and other charges for the sale, distribution, transmission and storage of gas, effective for the year commencing January 1, 2003. The Board assigned file number RP-2002-0130 to the Application. 16

The current application arises under a Performance Based Regulation ("PBR") methodology for setting rates approved by the Board in its RP-1999-0017 Decision with Reasons issued July 21, 2001. In the RP-1999-0017 Decision, the Board approved a three-year trial PBR plan under which rates would be changed for years commencing January 1, 2001, 2002, and 2003. 17

For the trial PBR plan, rates are adjusted using a price cap index ("PCI") determined by an inflation factor ("I"), a fixed factor of -2.5% reflecting a productivity target and input price differential ("X"), and certain pass-through items and non-routine adjustments. 18

1.2 The Proceeding 19

Union filed evidence in support of the Application on June 25, 2002. 20

Union outlined its prefiled evidence and received feedback from intervenors at a stakeholder consultation, held at the Board on August 7, 2002. 21

On August 22, 2002, the Board issued Procedural Order No. 1, setting out dates as follows: a Stakeholder Conference to be held on September 18, 2002 and September 19, 2002; an Issues Conference, September 25, 2002; an Issues Day, September 26, 2002; interrogatories on the Applicant's evidence, October 16, 2002; interrogatory responses, October 30, 2002; supplementary interrogatories on the Applicant's evidence, November 6, 2002; interrogatory responses, November 13, 2002; filing of intervenor evidence, November 18, 2002; interrogatories on intervenor evidence, November 25, 2002; interrogatory responses, December 2, 2002; submission of intervenors' position papers for the Settlement Conference, December 3, 2002; a Settlement Conference, December 5 - 13, 2002; and submission of any proposed Settlement Agreement to the Board on December 20, 2002. 22

A stakeholder conference held on September 18 and 19 provided intervenors with an opportunity for further discovery of Union's prefiled evidence. 23

Parties met to discuss a proposed Issues List at an issues conference held on September 25, 2002. 24

25

The proposed Issues List, containing five contested issues, was brought before the Board on issues day, September 26, 2002. After the Board heard parties' submissions on the contested issues, it rendered its decision in respect of the proposed Issues List; the Board determined that all of the contested issues except for "Weather Normalization" would be included on the Issues List in this proceeding. On September 30, 2002, the Board issued Procedural Order No. 2 containing the approved Issues List.

On October 28, 2002, Union filed updates to its evidence and a proposal for the elimination of the delivery commitment credit ("DCC"). 26

By letter dated October 29, 2002, Union informed the Board that it was unable to meet the deadline set out in Procedural Order No. 1 for responses to interrogatories (October 30, 2002) and requested an extension of this deadline to November 8, 2002. 27

In view of the additional evidence filed and Union's request, the Board issued Procedural Order No. 3 on November 1, 2002, amending the dates for the proceeding as follows: Union's interrogatory responses, November 8, 2002; supplementary interrogatories on Union's evidence, November 15, 2002; responses to supplementary interrogatories, November 22, 2002; intervenor evidence, November 29, 2002; interrogatories on intervenor evidence, December 9, 2002; interrogatory responses, December 16, 2002; intervenors' position papers and Board staff comments paper for the Settlement Conference, January 3, 2003; Settlement Conference, January 7 - 17, 2003; submission of any settlement proposal to the Board, January 24, 2003. 28

By letter dated November 27, 2002, the City of Kitchener requested an extension for filing intervenor evidence from the deadline of November 29, 2002, as set out in Procedural Order No. 3, to December 4, 2002. In response, on November 28, 2002, the Board issued Procedural Order No. 4 which amended the dates for filing intervenor evidence to December 4, 2002, for interrogatories on intervenor evidence to December 11, 2002, and interrogatory responses thereto by December 18, 2002. Procedural Order No. 4 did not amend any other dates in this proceeding. 29

1.3 The Settlement Conference 30

Board staff provided a summary of all the issues to all parties on January 3, 2003, prior to the commencement of the Settlement Conference. 31

Prior to the commencement of the Settlement Conference, Board staff received position papers from the following parties: Energy Probe, Ontario Association of Physical Plant Administrators, Vulnerable Energy Consumers Coalition, Wholesale Gas Service Purchasers Group, London Property Management Association, Canadian Manufacturers and Exporters, Enbridge Gas Distribution Inc., Coalition for Efficient Energy Distribution, Consumers Association of Canada, Industrial Gas Users Association, Direct Energy Marketing Limited, and the City of Kitchener. 32

A Settlement Conference, attended by the Applicant, interested parties, and Board staff, was convened on January 7, 2003, with Ms. Cindy Dymond acting as the facilitator. 33

Following the conclusion of negotiations on January 14, 2003, parties reconvened on January 17, 2003 to complete the drafting of the Settlement Proposal. The Settlement Proposal was submitted to 34 the Board on January 20, 2003. Parties had reached a complete settlement on twenty-five of the thirty-four issues on the Issues List.

On January 24, 2003, the Board issued Procedural Order No. 5, which set February 17, 2003 as the date for Union's presentation of the Settlement Proposal and set February 24, 2003, as the date to commence the oral hearing of Union's evidence. 35

Union made an oral presentation of the Settlement Proposal to the Board on February 17, 2003, following which the Board accepted it as proposed. The Settlement Agreement is attached as Appendix A of this decision. 36

1.4 The Oral Hearing 37

The remaining matters were examined in the oral hearing. The oral hearing of the unresolved issues commenced on February 24, 2003, and continued until March 3, 2003. 38

Union's written argument in chief was submitted on March 6, 2003. Intervenors' arguments were filed by March 11, 2003, and Union's reply argument by March 14, 2003. 39

1.5 Participants and their Representatives 40

Below is a list of participants and their representatives that participated actively, through the settlement conference process, leading evidence or cross-examining at the oral hearing, or by filing argument. 41

42

Union Gas Limited ("Union")	Michael Penny
	Marcel Reghelini
	Bryan Goulden
Board Counsel and Staff	Pat Moran
	James Wightman
Canadian Manufacturers & Exporters Inc. ("CME")	Malcolm Rowan
	Bruce MacOdrum
Coalition for Efficient Energy Distribution ("CEED")	George Vegh
	Robert Frank
Consumers' Association of Canada ("CAC")	Robert Warren
	Julie Girvan
The Corporation of the City of Kitchener ("Kitchener")	Alick Ryder
	Dwayne Quinn

Direct Energy Marketing Limited ("Direct Energy")	Ian Mondrow
Enbridge Gas Distribution Inc. ("EGDI")	Tania Persad
Energy Probe ("EP")	Frank Cianflone
Green Energy Coalition ("GEC")	David Poch
The Heating, Ventilation, Air Conditioning Contractors Coalition Inc. ("HVAC")	Brian Dingwall
Hydro One Networks Inc. ("HONI")	Glen MacDonald
Industrial Gas Users Association ("IGUA")	Peter Thompson
	Vince DeRose
London Property Management Association ("LPMA")	Randy Aiken
Ontario Association of Physical Plant Administrators ("OAPPA")	Valerie Young
Ontario Association of School Business Officials ("Schools")	Thomas Brett
Pollution Probe	Murray Klippenstein
	Jack Gibbons
Tractebel Power, Inc.	Richard King
TransCanada PipeLines Limited ("TCPL")	Tibor Haynal
Vulnerable Energy Consumers' Coalition ("VECC")	Michael Janigan
	Joyce Poon
Wholesale Gas Purchasers Service Group ("WGPSG")	Randy Aiken

The Board received letters of comment from the following parties: 43

PPG Canada Inc., Terra International (Canada) Inc., Stelco Inc., TransAlta Cogeneration L.P., and Dofasco Inc. 44

1.6 Witnesses 45

The following Union employees appeared as witnesses: 46

47

Steve Baker	Vice-President, Gas Supply
Steve Poredos	Director, Capacity Management
Dave G. Simpson	Manager, Asset Acquisition
Don Newbury	Manager, Integrated Supply Planning

Sarah VanDerPaelt	Manager, Product and Service Development
Mark D. Kitchen	Manager, Rates and Pricing
Dave Simpson	Manager, Asset Acquisition

Kitchener called the following witness: 48

Dwayne Quinn	Kitchener, Director of Utilities	49

VECC called the following witnesses: 50

John Todd	President, Econalysis Consulting Services	51
Joyce Poon	Consultant, Econalysis Consulting Services	

1.7 Submissions and Exhibits 52

Copies of the evidence, exhibits, arguments, and a transcript of the proceeding are available for review at the Board's offices. 53

The Board has considered the evidence, submissions and arguments in the proceeding, but has summarized the evidence and the positions of the parties only to the extent necessary to provide context for its findings. 54

The Board, with industry participation, has developed standards and processes for the electronic regulatory filing ("ERF") of evidence, submissions of parties, Board orders and decisions. This Decision with Reasons will be available in ERF form shortly after initial copies are issued in hard copy. The ERF version will have the same text and numbered headings as the initial hard copy, but may be formatted differently. 55

A list of abbreviations used in this Decision is provided in Appendix B. 56

2 2003 VERTICAL SLICE 57

2.1 Background 58

In its RP-1999-0017 Decision With Reasons, the Board approved a "vertical slice" methodology to allocate and assign the upstream transportation capacity held by Union to serve those system customers who migrate either to direct purchase or to an unbundled service during the term of Union's trial performance based regulation ("PBR") plan. 59

The vertical slice to be used in Union's Southern Operations Area is an annual proportional allocation of the assets in the upstream transportation portfolio for this area, as projected for November 1st of each year, based on the customer's Daily Contract Quantity ("DCQ") of the transportation, exchanges, and any other transport used to serve existing system customers moving to direct purchase. 60

The Southern operations system portfolio projected for November 1, 2002 consisted of 30.1% of TransCanada PipeLines Limited Firm Transportation ("TCPL FT") capacity, 46.8% of Alliance/Vector capacity and 23.1% of Trunkline capacity. Union proposed that this portfolio be used to allocate the transportation components for customers switching to direct purchase during the period of November 1, 2002 to October 31, 2003. 61

2.2 Inclusion of Northern and Eastern Operations Capacity 62

The TCPL FT capacity referred to above is Northern and Eastern Operations capacity ("Northern capacity") which is required to meet peak day requirements in the Northern and Eastern Operations area but, which is, on an annual basis, projected to be in excess of the forecasted annual demand. Union stated that it would continue to optimize the overall asset portfolio by filling the excess Northern capacity and diverting it on TCPL's system, as available, to Union's Southern Operations Area to serve system customers' demands. The delivery point for this capacity would be deemed to be Parkway. Because this TCPL capacity is not firm capacity to Parkway and the receipt point is Empress, Union proposed that this portfolio component not be assignable. 63

Union stated that its proposal would enable it to continue to operationally manage the diversion on TCPL as well as to operationally manage the peak day requirements in the Northern and Eastern Operations Area. Union's proposal would utilize the Northern capacity to serve the Northern and Eastern Operations Area during peak periods in this area. For non-peak periods in the Northern and Eastern Operations Area, the Northern capacity would be used to serve the Southern Operations Area to avoid unabsorbed demand charges ("UDC"). 64

Union submitted that the impact of assigning the Northern capacity to a Southern direct purchase customer would be that Union would have inadequate assets to serve the Northern and Eastern operations area and bundled direct purchase customers during peak periods. As such, under these circumstances, Union would be required to purchase additional capacity and perhaps a peaking service, which would create additional costs. 65

Union asserted that non-assignability of the Northern capacity would have no operational impact on direct purchasers because of the firm supplies provided by direct purchasers at Empress. Union added that its original RP-1999-0017 proposal did not contemplate that all components of the vertical slice would necessarily be assigned. 66

Union submitted that it was, for the first time, proposing to include the Northern capacity in the 2003 vertical slice, because northern diversions have assumed a larger role in the overall portfolio as available TCPL capacity to the south had decreased due to the migration to direct purchase. 67

Union stated that its proposed treatment of the Northern capacity was consistent with the approaches taken to the determination of the vertical slice in prior years. For example, the vertical slice proposed for November 2000 in the RP-1999-0017 proceeding included a proportional allocation of Union's exchange contracts. These contracts required the customer to deliver gas at Empress and receive gas at Parkway and were not assignable. Union stated that no complaints were made about the inclusion of the exchanges at the time and they were accepted by the Board as part of the vertical slice. 68

Union also stated that non-assignability of the Northern capacity would not tie the direct purchase customer to Union any more than any other upstream component ties a customer to Union. If a direct purchase customer did not want the Empress delivery arrangement provided by the diverted Northern capacity, the customer could post the capacity on Union's electronic transportation clearing house and exchange it for alternate capacity with direct purchase customers in Union's franchise area. 69

Union concluded that the issue was not whether it did, or did not, achieve the optimal operational utilization of its assets or did, or did not, think northern diversions were material enough to include in the vertical slice in a prior year. In Union's submission, the issue is whether northern diversions are part of the upstream portfolio used to serve the south. Since the northern diversions are in fact part of the upstream portfolio, Union argued that the capacity should be included in the vertical slice. 70

2.3 Exclusion of Delivered Supply (Spot Gas) 71

The proposed vertical slice does not include any spot gas. Union's rationale for this exclusion is that spot gas supplies do not flow on a 365 days per year basis and are by definition the most variable component in the utility portfolio. Union stated that the role of spot gas purchases is to provide it with the physical flexibility to serve the daily and seasonal balancing needs of all system and bundled direct purchase customers. 72

Union added that the basis of the vertical slice has always been a proportional allocation of its upstream transportation portfolio involving an obligation to deliver gas on a firm basis 365 days of the year: spot gas does not form a part of Union's upstream transportation portfolio and therefore is not part of Union's firm supply arrangements. 73

Union submitted that the only spot gas it purchases is for seasonal balancing and system optimization and integrity and that such gas is not acquired every day of the year. Union stated that if direct purchasers were responsible for all of their operational balancing needs, both at contract year-end and within the contract year, Union would include an allocation of its planned spot gas purchases in the vertical slice. 74

75
Union argued that the absence of spot gas from the vertical slice does not mean that customers do not have flexibility. Union noted that since the contracts underpinning 51.5% of Union's 2001 vertical slice expired on October 31, 2002, customers who migrated to direct purchase in the twelve-month period prior, achieved the flexibility afforded by spot purchases in their own supply portfolio as the arrangements expired. Similarly, Union noted that for the 2002 vertical slice, 23.1% of the contracts will expire on November 1, 2003.

76
Union submitted that including spot gas in the vertical slice would (i) restrict Union's ability to reduce discretionary purchases as a means of avoiding UDC, (ii) have negative effects on its balancing capacity since spot gas underpins this capacity, and (iii) increase its winter spot gas requirements as the management and control of any allocated spot gas would be removed from it.

77
2.4 Positions of the Parties

78
All parties except CEED accepted Union's vertical slice proposals for the year beginning November 1, 2002, subject to the conditions outlined in the Settlement Agreement. CEED argued that the Northern capacity included in the vertical slice should be assignable and that spot gas should be included in the 2003 vertical slice.

79
IGUA stated that the resolution of these issues depends on how the Board's prior decisions with respect to the vertical slice components are interpreted. In IGUA's view, Union has correctly interpreted and applied the Board's prior decisions.

80
VECC supported Union's proposal to assign the Northern TCPL capacity for the November 2002 vertical slice, since this allocation to direct purchase customers maintains the optimization of Union's system.

81
CEED submitted that the composition of the vertical slice is important because the purpose of the limited unbundling of transportation that has taken place is to assign the risk and reward of these assets to the marketplace.

82
CEED argued that Union's proposal attempted to obviate the limited unbundling approved by the Board and sought to rebundle transportation.

83
Regarding inclusion of Northern capacity in the vertical slice, CEED argued that Union had used this capacity in previous years in exactly the same way as it would after November 1, 2002, even though this capacity had not been included in the vertical slice previously. CEED noted that Union's prior exclusion of this capacity from the vertical slice had not prevented Union from operating in such a way as to avoid stranded pipeline demand charges in the North.

84
With respect to spot gas exclusion, CEED argued that Union had stated in the RP-1999-0017 proceeding that spot gas would be included in the vertical slice; however, Union was now seeking to redefine spot gas to include only delivered supply that arrives on a 365 day basis. CEED remarked that since spot gas is a forecasted component of the 2002/2003 portfolio, it should be included in the vertical slice.

Further, CEED stated that Union's purported requirement that only supply being delivered on a 365 85
day per year basis be included in the vertical slice is inconsistent with its attempts to include the Northern capacity in the vertical slice.

CEED described Union's proposal as opportunistic, inconsistent, and contrary to the direction that 86
Union has received from the Board. In CEED's view, rather than attempting to build more flexibility into its upstream transportation portfolio, Union's proposal attempted to foist transportation-backed contracts on direct purchase customers while withholding the most flexible portion of its portfolio for itself.

CEED concluded that the inclusion of the Northern capacity and the exclusion of spot gas from the 87
vertical slice constitute changes to the vertical slice methodology and should not be permitted. CEED argued that the methodology in place is interim and must be reviewed by the Board in time for the end of the 2003 interim approval period. CEED submitted that the appropriate time for the Board to consider approval of Union's current vertical slice ‟changes" would be when the Board reviews the methodology.

2.5 Board Findings 88

The Board notes that as part of the Settlement Agreement, all parties except CEED accepted Union's 89
vertical slice proposals for 2003 on the condition that, in the 2004 rate case, Union would provide (i) a full and complete description of the basis on which costs in the Other Purchased Gas Cost deferral account are classified as delivery related and (ii) Union's response to the Board's directive regarding load balancing and flexibility costs, including an identification of the components, if any, of Union's portfolio that are used for the purposes of balancing and flexibility.

The issues CEED has raised may indicate the need for further clarity and specificity in terms of the 90
criteria used to include or exclude sources of gas in future vertical slices. However, the Board notes that the adoption of CEED's proposals raises a potential for additional costs and the related issue of who would pay them. The Board has no evidence in this proceeding as to the magnitude of such costs, nor has it received any proposals as to how such costs could be assessed or managed.

The Board is also not convinced by CEED's argument that the Northern Capacity inclusion and spot 91
gas exclusion constitute changes in the vertical slice methodology.

Accordingly, the Board accepts the components of the vertical slice as proposed by Union for the 92
2002-2003 year. However, the Board will be open to further consideration of CEED's proposals in the 2004 proceeding, subject to a full assessment of all cost and related implications and how parties to the proceeding would propose that any such costs be allocated and recovered.

DECISION WITH REASONS

3 DELIVERY COMMITMENT CREDIT 93

3.1 Background 94

In the Western Accord on Energy Pricing and Taxation (the "Accord”) of March 28, 1985, the 95
Governments of Canada, Alberta, British Columbia and Saskatchewan recognized a need for more flexible and market-oriented energy pricing. Pursuant to the Accord, those governments signed the Agreement on Natural Gas Markets and Prices (the "Agreement”) on October 31, 1985. The basic principles underlying the Agreement included enhanced access for Canadian buyers to gas supply, enhanced access for Canadian producers to gas markets, protection for Canadian consumers for reasonable, foreseeable gas requirements, and commitment to foster a competitive market for natural gas in Canada. Although Ontario was not a signatory to the Agreement, the Board supported these basic principles in decisions made subsequent to the Agreement. The Board also indicated that it believed that open access to different sources of natural gas supply was essential to the development of the competitive market.

The implementation of the Agreement was left to the affected parties. The Agreement stated: 96

> "Effective November 1, 1985, consumers may purchase natural gas from producers at 97
> the negotiated prices, either directly or under buy-sell arrangements with distributors, provided distributor contract carriage arrangements are available in respect of such purchases. This provision is in no sense intended to interfere with provincial jurisdiction in regard to regulation of gas distribution utilities.”

Direct Purchase was defined as an arrangement whereby an end-user of natural gas purchases gas 98
directly from a producer or broker rather than from a local distribution company ("LDC”). The gas was transported to Ontario by TCPL and handled by the LDC in one of two ways: (i) Buy-Sell, wherein the Ontario LDC purchases the direct purchaser's volumes, commingles them with other purchased gas and sells to the direct purchaser as a sales customer under the appropriate rate schedule; or (ii) Contract Carriage, wherein the LDC does not take title to the direct purchaser's supply of gas but contracts to carry the volumes of gas from the point of receipt through the LDC's system to the direct purchaser's take-off point.

The period from November 1, 1985, to October 31, 1986, was designated as transitional to a market 99
pricing regime during which wholesale prices prescribed by governments were frozen, but industrial customers without gas sales contracts with the LDCs were free to negotiate natural gas purchase prices directly with producers, conditional upon contract carriage arrangements being available from the LDCs.

On December 9, 1985, on its own motion under docket numbers E.B.R.O. 410, 411, and 412, the 100
Board called proceedings to deal with interim contract carriage arrangements on the distribution systems of Consumers’ Gas, ICG, and Union. The hearings were combined and commenced on January 27, 1986.

101

In the EBRO 410/411/412 proceedings, Union proposed that Oakville be the only delivery point for direct purchase deliveries allowed on its system, arguing that a direct purchaser's failure to deliver full daily volumes at Oakville could result in an inability to serve all firm customers, even if the failing direct purchaser were curtailed. In its Reasons for Decision issued on April 4, 1986, the Board, while recognizing the impacts on parties of the choice of delivery points, expressed concern that allowing the utilities to designate delivery points could impair development of transportation services and exclude entry of gas from the U.S. The Board directed Union not to mandate Oakville as the delivery point for the interim period but rather treat the issue on a case-by-case basis (with the Board as the arbiter in the event of dispute) "... in order not to discourage potential T-service customers." The Board added that buy/sell arrangements were "a viable alternative to, and compatible with T-service," and determined that gas purchased by a utility under a buy/sell arrangement would be at a rate no higher than the utility's avoided commodity cost.

102

On its own motion, the Board called further hearings, commencing in September 1986 under docket number EBRO 412-II, to deal with contract carriage and direct purchase arrangements. Union submitted that T-service availability would be contingent on acceptable arrangements to ensure system integrity; if such arrangements could not be made, Union proposed that the following terms and conditions of T-service be mandatory: (i) Oakville-only deliveries, (ii) delivery of full TCPL contracted demand on any critical day, (iii) confirmation of the customer's upstream supply arrangements, and (iv) requirement that the customer contract for firm TCPL and NOVA service. Union stated that firm supply delivered at Oakville was used to meet Union's obligations to M12 customers; failure of delivery of forecast supplies at Oakville would require Union to make up the shortfall by transporting volumes the length of the Dawn-Trafalgar system, a usage for which the transmission system facilities were not designed. Union argued that the direct purchaser alone should bear responsibility for security of supply and proposed backstopping, proportional reductions in its transmission obligations, FST displacement, and increased facilities as potential solutions.

103

In its Reasons for Decision issued on March 23, 1987, the Board found that it would not require an obligation to deliver as a condition of a T-service contract and "... that without such an obligation, the failure of a direct purchaser on a peak day to deliver its gas could result in a penalty to the direct purchaser, unless matched with an equivalent reduced take. The Board finds that there should be no difference in this regard between a T-service contract and a buy-sell arrangement." The Board again found that the delivery point should be negotiated by the parties; absent resolution, the Board would decide. The Board added that core market supply should be ensured by the LDC by prudent and necessary contractual arrangements.

104

In the EBRO 412-III proceeding, Union submitted that it should have right of first refusal for a direct purchase customer's TCPL capacity upon expiry of the direct purchase contract. Union also proposed that its Weighted Average Cost of Gas ("WACOG"), rather than the avoided cost of gas, be paid for buy/sell supplies for two reasons. First, to reduce the utility's cost of gas and, secondly, to eliminate the incentive for customers to choose buy/sell over T-service. Regarding security of supply , Union stated that it had arranged with TCPL to maintain firm deliveries through TransCanada's northern leg in the event of a shortfall. In its Reasons for Decision issued May 27, 1988, the Board denied Union's proposal to have a right of first refusal to TCPL capacity, noting that a Direct Purchase customer could not be guaranteed re-entry to the sales service class. The Board also found that a buy/sell customer should not be obligated to deliver, since a T-service customer was not so required. In addition, the Board found that Union's WACOG was an appropriate "buy" price for an Ontario buy/sell for either a customer without an obligation to deliver and for whom Union was not required to provide firm sales service or a customer who accepts an obligation to deliver and demands firm sales service. The Board confirmed its earlier findings with respect to mandated delivery points.

In the EBRO 456-4 proceeding, Union proposed that the buy/sell purchase price for obligated supply be based on Union's weighted average price of firm supply, that is, at a premium to the buy/sell purchase price for unobligated supply which was based on Union's WACOG. In its Reasons for Decision issued April 14, 1989, the Board found that all buy/sell customers should obligate to deliver on a firm basis and Union's weighted average cost of firm gas purchases should be used for all buy/sell arrangements. 105

In the EBRO 456 proceeding, Union proposed that interruptible T-service customers be obligated to have firm upstream arrangements and deliver at 100% load factor. In its Reason for Decision issued September 26, 1989, the Board declined to extend the obligation to deliver to interruptible T-service customers. 106

In its Reason for Decision in EBRO 462, issued April 9, 1990, the Board accepted Union's proposal to pay a delivery commitment credit ("DCC") to T-service customers who obligated to deliver firm gas under the new R1 rate schedule. This approval was granted on a trial basis for the test year. 107

In the EBRO 493/494 proceeding, Union proposed that (i) existing buy/sell customers receive a price based on three one-year fixed price quotes plus the TCPL toll, and (ii) new buy/sell customers receive a price based on a blend of the price received by existing buy/sell customers for the volumes underpinned by firm TCPL and the one-year forward price of delivered gas for the remaining supply. In its Reasons for Decision issued March 20, 1997, the Board found that the Alberta border forecast WACOG should be used as the basis for all new buy/sell contracts and for existing buy/sell contracts upon renewal. 108

In the EBRO 493-04/494/06 proceeding, Union proposed to pay a delivery commitment credit ("DCC") to buy/sell customers to restore equality between T-service and buy/sell service. Union also proposed to change the methodology used to allocate delivery commitment credit costs to in-franchise customers based on deliveries of volumes to Dawn-Trafalgar and design day demand. In its Reasons for Decision, issued February 10, 1998, the Board stated: 109

> "The Board agrees that there is a necessity for a thorough review of matters related to payments for firm deliveries, and directs that this review take place in the next main rates hearing. The Board expects evidence in that hearing to address new approaches to these matters, including possible penalties for non-delivery, possible variations related to the value of the deliveries during different seasons and to different receipt points, or possible alternative incentives to ensure firm delivery. ... In the interim, the Board accepts Union's proposal that buy/sell customers receive a payment equivalent to the DCC paid to T-service customers and that the costs be allocated based on peak day demand and storage space as proposed." 110

In the EBRO 499 proceeding, Union brought forward the following alternatives: (i) continue paying the current DCC; (ii) pay a DCC based on avoided incremental transmission facilities costs; (iii) pay a DCC based on avoided transmission facilities, costed at average existing embedded costs; (iv) pay a DCC based on avoided incremental storage and transmission facilities costs;(v) pay a DCC based on avoided storage and transmission facilities, costed at average existing embedded costs; (vi) stop paying a DCC and request that all deliveries be obligated; and (vii) stop paying a DCC and require that all deliveries be obligated and implement penalties for unobligated deliveries. 111

Union provided an analysis of these seven options in its pre-filed EBRO 499 evidence and then 112
proposed the following as its preferred option: that it continue paying a DCC on obligated deliveries and base the rate on the existing M12 storage and transportation rates to recognize avoided transmission and storage facilities. The effect of Union's proposal was to raise the DCC payment from $3.88/10^3m^3 to $4.25/10^3m^3. In the Settlement Agreement, dated November 16, 1998, parties accepted Union's proposal. The Board accepted the Settlement Agreement at the commencement of the oral hearing in the EBRO proceeding and the Settlement Agreement was attached as Appendix B to the Board's Decision With Reasons issued on January 20, 1999.

In the RP-1999-0017 proceeding, parties to the Settlement Conference agreed that "[t]he DCC will be 113
eliminated in a manner which is revenue neutral to all end-use customers." Parties agreed to defer the elimination to coincide with the projected (small volume) unbundling implementation. The Settlement Agreement, dated June 7, 2000, was accepted by the Board and was attached, as Appendix D, to the Board's Decision With Reasons issued July 21, 2001.

In the RP-2001-0029 proceeding, some parties disagreed with Union's proposed rate adjustments 114
implementing DCC elimination. Concerns were raised with respect to the revenue neutrality and the resultant revenue-to-cost ratios of Union's proposals. In its Decision With Reasons, issued September 20, 2002, the Board found, *inter alia*:

> While the Board is reluctant to stray from the terms agreed to in an accepted 115
> settlement agreement, the Board notes that in this case there appear to be differences of view among the parties to the Settlement Agreement in RP-1999-0017 as to the meaning of "revenue neutrality". The wording of the agreement would itself indeed permit more than one interpretation of how revenue neutrality is to be satisfied. Furthermore, Union and IGUA, both support retention of the DCC in its current form, absent the elimination under the terms of revenue neutrality proposed by Union. (Para. 6.85)
>
> The Board therefore finds it appropriate to defer the elimination of the DCC until 116
> Union brings forward a proposal that addresses the issues and concerns as stated above and an implementation plan. If the rate impact of discontinuing an allocation of "credit" to the large industrial classes would be large enough to materially affect gas deliveries to large customers, the proposal should address a phasing out of the credit program over time. (Para. 6.86)

In the current proceeding, Union proposed that, for each rate class, the DCC payment be eliminated 117
and delivery rates be lowered by the amount of the foregone DCC payment. Union submitted that its proposal was the same as originally proposed in RP-1999-0017.

Union stated that the DCC is paid by Union to direct purchase ("DP") customers for firm, daily 118
deliveries at a specified point on Union's system. Union said it relies on these deliveries in designing distribution, transmission, and storage facilities to meet design day demands of all customers. Further, deliveries obligated at a fixed delivery point means lower-than-otherwise facilities' costs and hence lower rates for all customers.

119

Union noted that all witnesses agreed that Union needs to know where DP deliveries will be made and needs a significant level of obligated deliveries at Parkway to avoid Dawn-Trafalgar ("D-T") expansion costs and also that DP obligated deliveries at Parkway provide a system benefit of avoided D-T facilities costs.

Union stated that since the early days of commodity deregulation, the Board has prohibited Union 120
from unilaterally requiring Parkway deliveries for fear of impairing development of a competitive DP market. However, the obligated Parkway deliveries avoid D-T expansion costs.

Union submitted that the Board, recognizing the benefits of obligated deliveries to a fixed point, 121
approved Union's payment of a premium to incent DP customers to contract for obligated Parkway deliveries and to recover the cost of these payments in rates. Union stated that the premium has been called the DCC since 1990 and been based on avoided D-T transmission facilities' costs since 1998.

Union argued that, with the singular exception of M2 customers, its proposal is revenue neutral for 122
each class with respect to net bills before and after DCC elimination. For M2 customers, the DCC credit of $3.8M was paid to marketers and therefore it did not appear as a line item credit on their bills. Union's proposal would lower M2 delivery rates by $3.8M and hence provide a net benefit of $3.8M.

Union argued that the Board had not allowed Union to unilaterally impose a Parkway delivery 123
requirement in its EBRO 412-I Decision due to the Board's concern over inhibiting the development of a competitive commodity market in Ontario. The Board reaffirmed this in EBRO 412-II and EBRO 412-III stating that the delivery point be negotiated between Union and the buy/sell or T-service customer.

Union stated that in EBRO 412-III, the Board approved the payment of a premium to buy/sell 124
customers who obligated deliveries to a fixed point, above the weighted average cost of all supplies paid for non-obligated buy/sells. Union submitted that the Board thereby explicitly recognized "... the financial benefit provided by the direct purchaser who agreed to obligate its deliveries to Parkway."Union also submitted that the Board found that the buy price for unobligated deliveries would be less than the buy price for obligated deliveries.

Regarding the Board's finding, in the EBRO 456-4 Decision, that buy/sell customers who repurchase 125
gas from Union under firm sales service rates should supply gas on a firm basis, Union claimed that the context of the Decision was that Union could not mandate DP deliveries at Parkway and that "obligated deliveries to a fixed delivery point received a premium payment over non-obligated deliveries."

Union submitted that the term "Delivery Commitment Credit" was first used in EBRO 462. The Board 126
found the premium should be extended to contractually obligated T-service customers to provide them with the same incentives as buy/sell customers.

Union asserted that although in EBRO 493/494 the premium for obligated buy/sell deliveries was 127
temporarily suspended, in EBRO 493-04/494-06 the Board accepted Union's proposal that buy/sell customers receive a payment equivalent to the T-service DCC payment and that the costs be allocated based on peak day demand and storage space.

In response to a Board directive made in EBRO 493-04/494-06, in the EBRO 499 proceeding Union proposed that the DCC be retained for obligated deliveries and also that it be calculated using existing M12 rates, based on the avoided cost of storage and transmission facilities. The latter change increased the DCC payout to $\$4.25/10^3m^3$ for a total cost of approximately $27 million. Union noted that its proposal was accepted in the EBRO 499 Settlement Agreement and approved by the Board. 128

In the RP-1999-0017 proceeding, Union proposed to convert the DCC payment into a rate reduction such that the net delivery bill pre- and post-implementation of the proposal would be the same. Union noted that the proposal was agreed upon in the RP-1999-0017 Settlement Agreement and accepted by the Board. Union stated that because the RP-1999-0017 Decision was received in July 2001, implementation of the change with respect to the DCC was deferred until the next proceeding, RP-2001-0029. 129

Union asserted that the first time that intervenors argued "... that what they thought they had agreed to in respect of the DCC in RP-1999-0017 differed from what Union was proposing. In the end, the Board in RP-2001-0029 found that there had, in fact, been no agreement on the issue and held that the DCC should continue and that Union should bring forward a proposal on the DCC that would be reviewed by the Board and decided upon in this case." 130

Union stated that its current proposal (i) "continues to recognize the system benefits provided by direct purchase customers who obligate deliveries at Parkway ..."and (ii) is revenue neutral to customers. 131

Union argued that it designs Dawn-Trafalgar facilities to meet demands on a design day, i.e., a 44-degree day on which all interruptible customers have been interrupted. Because the facilities' costs are caused by customers' use on a design day, Union allocates Dawn-Trafalgar facilities costs to classes in proportion to the design day demands of each customer class. Union submitted that "[t]he cost to Union of paying the DCC was incurred to avoid Dawn-Trafalgar costs ..." and "... the allocation methodology ... and its justification based on avoided facilities was explicitly proposed and approved by the Board ... in EBRO 493-04/494-06." 132

Union noted that the DCC payments are made monthly for each GJ of obligated delivery made during the month. Union stated that while M2 customers use 70% of the Dawn-Trafalgar capacity on design day, the M2 class only provides 14% of obligated deliveries, in contrast to M7 and T1 classes which together use 16% of facilities on design day but provide 61% of obligated deliveries. Union attributed these differences to the fact that general service M2 customers are heat sensitive and have a low load factor and also that only 40% of small volume customers are direct purchasers who obligate deliveries to Parkway. 133

Union described VECC's proposal as ending DCC payments to all direct purchasers, removing the $27 million in DCC costs from rates, and reducing each classes' rates by the DCC cost allocated to it. In Union's view this approach would not recognize the system benefits from obligated deliveries and would end "the Board's long-standing prohibition against unilaterally imposing delivery point requirements on direct purchase customers." Union submitted that VECC's proposal would replace the incentive DCC payment with the failure-to-deliver penalty, thereby subsidizing small volume customers at the expense of higher load factor contract customers. Union argued that VECC's real issue was with cost causation principles reflected in rates since EBRO 493-04/404-06. 134

Union asserted that VECC’s proposal would result in "massive transfers,” citing evidence that, under it, M7 and T1 rates would increase by 36% and 49% respectively while M2, M9, and M10 rates would decrease by 4%, 3%, and 10% respectively. 135

Union asserted that sales customers are advantaged in that they pay a regulated commodity rate, do not arrange for their own supply, and have no obligation to deliver. In contrast, direct purchasers do not pay a regulated commodity rate, arrange their own gas supply, and are obliged to deliver. Union added that direct purchasers contract with Union for storage and delivery services only, and are obligated to deliver on a daily basis regardless of daily consumption, and are subjected to a requirement to balance annually within 4%. Further, a failure to deliver exposes direct purchasers to DCC clawback and penalties. Union contended that while sales customers enjoy the avoided cost benefits provided by the direct purchase customers, they provide no avoided cost benefit at all.” 136

Union submitted that it has no obligations, to itself or any other entity, to deliver firm gas at a specified point, adding that "[n]one of the deliveries of gas Union arranges in respect of sales service customers are obligated to any delivery point in any way. Union arranges for supply and moves that supply to where it is needed on any given day.” Union cited its use of northern TCPL capacity to deliver gas to the southern area on a non-peak day as an example of the unobligated nature of its arrangements. Union remarked that spot gas balancing supplies are similarly not obligated as the gas is not delivered unless needed. 137

Union dismissed the argument that, under VECC’s proposal, delivery rate impacts on industrial customers are insignificant compared to the inherent commodity price volatility. Union also observed that average delivery rate increases of 36% to 49% would be a serious concern for VECC if such increases were being proposed for general service customers. Union noted that VECC provided no evidence that impacts on industrial customers would be insignificant under VECC’s proposal. Union continued that it does not know what industrial customers pay for gas, pointing out that while volatility is usually measured using day-to-day spot prices, industrial customers typically make longer-term arrangements for commodity using swaps, hedges, or similar agreements to mitigate price volatility. Union submitted that the proper concern for the Board in this matter is delivery rate impact as all customers are exposed to commodity price volatility. Further, for assessing the competitiveness of gas, the volatility of the price should be compared with the volatility of other fuels. 138

Union denied that its proposal was motivated by load retention considerations, suggesting that these considerations arise under VECC’s proposal. Union stated that load loss would be of concern should gas service become relatively less economic with respect to substitute fuels. Union referred to the evidence that it lost approximately $7.1 million in margin in 2001 due to fuel switching, noting that load losses would drive rates higher. In addition, expansion projects deferred due to the economics of natural gas as a fuel choice should also be expected to give rise to higher rates. 139

Union emphasized that rate design requires more than a cost assessment in determining whether rates are just and reasonable, citing overall sufficiency/deficiency, relative rate changes, how costs are allocated, rate levels and proposed changes, customer impacts, customers’ expectations with respect to rate stability and predictability, and equivalence of comparable service options as essential factors to be considered in rate design. 140

Union argued that its proposal took account of the attributes of a sound rate structure specified by Bonbright in his work on rate design. In Union’s view the proposal simplified the rate schedule, 141 minimized rate shock, considered customers' expectations, and addressed the comparability of equivalent service options. With respect to comparability of equivalent service options, Union stated that its DCC proposal was motivated partly by recognizing that future customers of unbundled services approved in RP-1999-0017 would provide the same avoided cost benefit as bundled direct purchasers by the 22-day Parkway call but would not be paid the DCC. In recognition of this circumstance, such customers would pay delivery rates net of the DCC. As such, Union submitted that its proposal treated equals equally.

142

Union agreed with the "small volume intervenors" that its proposal left "residual" DCC costs in rates, asserting that this feature recognized cost causation and rate design principles, reflecting differences among rate classes (i) in the provision of avoided cost benefits and (ii) in design day use of transmission capacity.

143

Union strongly urged the Board not to further defer the DCC issue, arguing: (i) the issue has been before the Board on three occasions, in the RP-1999-0017, RP-2001-0029, and the current proceedings; (ii) deferral of a decision on this issue will have only negative impacts, already being felt in customer negotiations, due to uncertainty with respect to the economics of new industrial loads; and (iii) the evidence is clear and complete on this issue.

144

3.2 Positions of the Parties

145

VECC submitted that the Board's three major findings with respect to the DCC issue in its RP-2001-0029 Decision with Reasons were: (i) the DCC was not required as an incentive for obligated deliveries, penalties may be a "significant encouragement"; (ii) Union's proposal was not acceptable without more compelling evidence; and (iii) if fuel switching in response to eliminating the DCC credit would be material, Union should bring a proposal that addressed phasing out of the credit program over time. VECC noted that Union's current proposal largely recapitulated the same position as in the RP-2001-0029 proceeding, in spite of the Board's "clear language" in the RP-2001-0029 Decision. Further, no phase out timetable had been proposed nor had Union provided evidence supporting the DCC as a load retention rate. Therefore, VECC submitted that it was open to the Board to find that since no new or compelling evidence had been presented by Union regarding the DCC, the DCC payments and costs be removed at once, or over time. Further, VECC charged that Union gave "short shrift" to Union's own ability to mitigate impacts through negotiated rates adding that "[b]ecause of the application of the PBR price cap, a direct rates subsidy from system sales customers in the form of embedded DCC costs is obviously more attractive to the Company, even if more flimsily supported."

146

VECC, LPMA, Schools, and CAC submitted that Union had not been responsive to the Board's RP-2001-0029 direction but merely refiled its original, RP-1999-0017 proposal.

147

VECC argued that the DCC should be eliminated completely from rates on the basis that existing contractual commitments and penalties should provide appropriate incentives to obligate deliveries.

148

VECC stated that since the new unbundled services did not require firm daily obligated deliveries, the DCC payment was now inconsistent with obligations requiring equal daily deliveries.

149

VECC was concerned that Union's proposal would result in rate reductions to large volume customers regardless of whether deliveries were obligated, or of migration to system sales service in the future. VECC noted that there was no contractual obligation for existing DP customers to remain DP customers beyond their existing one-year contract.

150

VECC submitted that DP customers' obligation to deliver be treated in the same manner as other system optimization practices which Union is responsible to undertake to achieve the lowest possible rates for all customers. Further, Union's proposal optimizes the system at a higher cost than pre-DP since the cost of the rate subsidy was not required prior to the innovation of Direct Purchase.

151

VECC criticized Union's proposal as not recognizing the system benefits provided by firm deliveries arranged to supply system sales customers. VECC remarked that Union's attribution of system benefits to some classes and not others for tasks performed by the utility pre-DP, was not consistent with the integrated system concept adopted by Union. VECC argued that Union's position selectively credited some classes of customers at the expense of others by considering system sales demands as day-to-day deliveries.

152

VECC noted Mr. Kitchen's testimony to the effect that if DP customers did not deliver as Union had, additional facilities would be required, the cost of which would be allocated to other customers based on Dawn-Trafalgar design day demand. Accordingly, VECC argued that costs caused by some customers would be allocated to other customers. This violation of cost causality principles would be exacerbated by the fact that the cost-causing DP customer would realize lower commodity prices while the system sales customer would paying for an avoided facilities cost embedded in rates plus a new, additional facilities cost.

153

VECC submitted that the design day methodology is used to allocate existing facilities, contending that Union's approach does not recognize or define which customers among all classes of customers cause additional facilities costs. Also, VECC noted that the Board in EBRO 470 held that it would ensure fair treatment of customers if DP migration increased costs.

154

VECC further criticized Union's proposal because the avoided costs built into rates would not change regardless of the quantum of avoided costs benefits provided.

155

VECC submitted that DP customers had voluntarily assumed the burden of making delivery arrangements in exchange for a lower gas supply cost and thus needed no additional subsidy. In addition, there was no evidence of an increased burden by obligating firm deliveries; rather, Union's witness stated that firm deliveries were more cost effective than interruptible deliveries.

156

VECC noted that existing direct purchasers have been able to turn back TCPL capacity allowing them to deliver gas at a lower cost than firm deliveries on the Alliance and Vector pipelines whose costs are the responsibility of system sales customers. Also, direct purchasers receive the DCC payment regardless of delivery point and enjoy some flexibility due to the ability to change delivery points from Parkway to Dawn while Union's deliveries on behalf of system sales customers are all at Dawn because Union has allocated all of its TCPL capacity to direct purchasers.

157

VECC suggested that if Parkway deliveries by DP customers were genuinely considered to be relatively onerous, the Board could find, as a least cost alternative to system optimization, that direct purchasers be able to change their delivery point to Dawn, provided that the DP customers choosing to do so assumed contractual commitments on the Alliance and Vector pipelines.

158

VECC disputed that Union's proposal was consistent with past practice, arguing that according to Union's witness, Mr. Kitchen, prior to EBRO 493-04/494-06 the DCC reflected the buy/sell methodology and was not embedded in rates. Mr. Kitchen also confirmed that the buy/sell mechanism arose due to Union's need to take title of a direct purchaser's gas; the buy/sell reference prices were in rates to facilitate the development of a competitive gas market.

159

VECC submitted that DCC payments recognizing avoided storage and transmission facilities costs started after the EBRO 499 Decision. Prior to EBRO 493-04//494-06, different commodity prices were paid by Union for obligated and non-obligated deliveries with the differential reflecting price, delivery point (Alberta or Ontario), and the transportation utilization underpinning delivery. Prior to the 1998 Act, when the utility had to hold title to the gas, buy/sell customers received a benefit due to the difference between the price they had negotiated with producers and the higher price in rates that Union paid to buy/sells.

160

VECC argued that in its EBRO 493/494 Decision with Reasons, the Board eliminated the price differential between obligated and non-obligated deliveries. The Board, in calling for changes to Union's buy/sell pricing methodology, noted that Union recorded deviations from the forecast cost of short-term supplies-- included in gas commodity charges for both buy/sell and system customers–to its PGVA "... which costs are usually charged only to system customers." In eliminating the differential, the Board commented that "... once this change is effected Union's own western Canadian firm supplies would not be excessively depleted due to an artificial economic incentive to elect direct purchase."

161

VECC submitted that the Board's findings in EBRO 493/494 more closely matched Union's actual firm supply costs with the costs paid to buy/sells by eliminating "... the higher cost of short-term supply embedded in the firm buy/sell reference price." VECC claimed that Union's prior practice under the Direct Purchase Displacement Policy increased commodity prices for system customers. VECC added that the Board also directed Union to bring a proposal to the Board for a commodity price for obligated deliveries that was closer to a true firm delivery price. VECC described Union's response to this directive (in EBRO 493-04/494-06) as "... the DCC with its current characteristics ... an artificial economic incentive to direct purchase customers based upon Union's unique view of system benefits." While the Board gave interim approval to the proposal -- pending a comprehensive review in the next proceeding -- there was no Board scrutiny of the DCC in the next proceeding because a comprehensive settlement agreement was filed with the Board.

162

VECC disputed Union's interpretation of the history of this issue, claiming: (i) no mention was made of either a reward for obligated deliveries or of the DCC as a premium for Parkway deliveries in EBRO 493/494; (ii) in EBRO 456-4, the Board required all deliveries (including DPs) to Ontario Local Distribution Companies (" LDCs") to be firm and obligated. The Board neither required Union to pay a premium for DP obligated deliveries nor recognized Parkway deliveries as qualifying for a premium; (iii) notwithstanding Union's claim that the Board's EBRO 412 decision precludes Union from mandating a delivery point, Union's contracts with DPs require obligated deliveries. Further, the EBRO 410-II, 411-II, and 412-II Decisions were issued prior to the existence of the current competitive gas market.; (iv) EGDI has included an obligated delivery requirement for its DP customers since EBRO 410-II and the following decisions, yet makes no payment similar to the DCC in recognition thereof; and (v) the EBRO 410-II and subsequent decisions considered the use of penalties-- not premia--to incent obligated deliveries. Regarding the finding that the delivery point be negotiable, again the Board did not propose a premium payment to the customer.

VECC cited evidence in the proceeding which supported an estimated end-use impact of 1%-2% if 163
DCC costs were removed from rates, arguing that "[t]he delivery rate change is small as an end use impact upon affected customers." VECC questioned Union's fear of load loss resulting from VECC's DCC proposal, noting that gas is currently competitive with oil and that existing firms have invested heavily in natural gas infrastructure. VECC also cited Union's admission that the greatest amount of fuel switching occurred during 2001, when commodity prices were rising".

With respect to interruptible loads, VECC suggested that under Union's scheme, residential customers 164
could end up paying DCC to keep load, without any assurance that load will be retained.

VECC stressed the comparison between the lost delivery margin of $7.1 million on interruptible 165
loads, and the avoided facilities benefit of $27 million. Even if a "speculative" loss of $7.1 million is included, VECC argued that its approach of eliminating the DCC based on costs, utilizing penalties, and keeping contractual delivery obligations was a least-cost optimization based on the evidence.

To mitigate the impacts of its proposal, VECC suggested that Union could negotiate load retention 166
rates and also phase out the DCC over a two- or three-year period.

VECC noted that the range of revenue to cost ratios would change, from 1.022 to 0.511 in EBRO 499, 167
to 1.06 to 0.295 under Union's proposal. Under VECC's proposal, the range would mirror the EBRO 499 range. VECC questioned the validity of Union's proposal given that no other jurisdiction had incorporated a similar methodology that transferred system benefits from one class to another in its rate design to recognize avoided facilities costs. VECC argued that "[i]f direct purchase customers get a credit for gas deliveries formerly made by Union before Direct Purchase came to be, then it is important that other types of benefits are recognized and similarly rewarded." Referring to the increased benefits to direct purchase customers arising from Union's Alliance and Vector contracts that allowed direct purchasers the benefits of turning back TCPL capacity and purchasing gas in the secondary market-- while not assuming the cost of the Alliance and Vector capacity, VECC asserted that consistency in rate design would require lower system customer rates in consequence.

LPMA accepted and supported VECC's evidence. 168

LPMA argued that the DCC payments are a real cost to Union that is recovered from in-franchise 169
customers in delivery rates. As such, when the payment of the DCC is eliminated, the cost should be removed from delivery rates.

LPMA submitted that "... the Board disallow any subjective rate adjustments by Union based on 170
perceived benefits to the system and/or avoided costs."

LPMA urged that the Board require that Union undertake any contractual arrangements, including 171
obligations to deliver in the absence of DCC payments or embedded rate reductions necessary to maintain system integrity at least cost.

172

LPMA accepted Union's evidence in respect of the need to eliminate the DCC and urged the Board not to defer a decision on this issue. LPMA noted that elimination of the DCC would eliminate the accumulation of related further debits in the Direct Purchase Revenue and Payments account.

LPMA disputed Union's contention that the Board's EBRO 412 decision prohibited Union from mandating the obligation to deliver, citing the Board's EBRO 412-II Decision that "a failure to deliver on a peak day could result in a penalty to the direct purchaser and that the core market be protected and the LDC may make whatever contractual arrangements are necessary and prudent." 173

LPMA noted that in EBRO 456-4, the Board found that all buy/sell volumes to Ontario LDCs should be firm and obligated and that Union should use the weighted average cost of firm supplies to determine the buy/sell cost of gas. LPMA argued that the EBRO 412-II and 456-4 decisions demonstrated that direct purchasers had an obligation to deliver and payment was based on Union's firm gas costs: direct purchasers' incentive was due to the difference between Union's firm gas price paid to them and the direct purchaser's actual cost of gas, completely unrelated to avoided facilities costs. 174

LPMA noted the testimony of Union's witness that after the elimination of the DCC payment, the associated cost would not appear in the cost allocation study. LPMA submitted that the $27 million currently in costs should be removed from rates on the basis of the current cost allocation methodology. 175

LPMA agreed with VECC that Union had failed to show any extra onus arising from direct purchasers' obligations to deliver, compared to Union's firm deliveries on behalf of system customers. Although Union admitted that both types of deliveries provide significant system benefits in terms of avoided facilities, LPMA cautioned against adjusting rates based on presumed system benefits, noting that difficult issues arise in selecting which benefits ought to be adjusted for and how they should be quantified. LPMA urged the Board to decide this issue based on an approved cost allocation methodology that reflects only the cost causality of actually incurred costs. As an example, LPMA stated that while it was reasonable to expect that the recent transfer of Union's S&T marketing function to DEGT would result in savings i.e., avoided costs, Union had not brought forward a proposal to recover these avoided costs from C1 and M12 customers and provide a credit to other classes. 176

Regarding avoided facilities costs, LPMA argued that if additional facilities are required in the future, M2 customers would pay for the bulk of new facilities and questioned why M2 customers should pay now for facilities not built and pay again for them when they are built. 177

LPMA added that there was no evidence that any other North American gas utility allocated avoided costs, nor, by Union's evidence, were any other avoided costs included in rates. The inclusion of avoided costs in rates moves the utility away from cost-based rates and raises the possibility of shifting real costs, which comprise the revenue requirement. 178

LPMA noted Mr. Kitchen's testimony that significant volumes were lost when the commodity price of gas spiked, resulting in a lost delivery margin of $7.1 million. LPMA questioned the rationale for including $15 million in M2 delivery rates to try and keep $7.1 million in margin, especially when there is no guarantee of retention in the face of commodity price changes. Based on Union's evidence, 179

LPMA contended that the least cost alternative to maintain obligated direct purchase volumes is therefore $7.1 million, not the $27 million proposed by Union.

LPMA cited the testimony of Union's witnesses, that direct purchasers moving obligated deliveries from Parkway to Dawn are required to buy a service to move molecules from Dawn to Parkway. If additional facilities were required to facilitate this delivery point flexibility, the customer causing the incremental costs, would be responsible for the additional facilities costs. Union's testimony was that new contract customers, whose service required additional facilities, would have to pay for those facilities either through rates or an aid-to-construct payment. LPMA argued if a customer's action to not obligate deliveries increases facilities' requirements, this same customer should bear the cost responsibility: "A customer's action should not lead to incremental costs for other in-franchise customers." 180

Based on the evidence, LPMA suggested a three-year phase-out period would be appropriate, arguing that a longer phase-out period would be onerous on M2, M9, and M10 customers. 181

LPMA noted that, based on Union's gas commodity cost of $237.99/10^{3}m^3, the evidence indicated that VECC's DCC proposal would increase end use costs to the contract rate classes by 1% - 2%. Conceding Union's point that contract customers may pay a different commodity price than Union, LPMA remarked that even if direct purchasers paid 25% lower commodity prices than Union, the maximum end use rate impact of VECC's proposal was 3% in total or 1% annually over a three-year phase-out period. 182

Schools supported VECC and LPMA in that direct purchasers' delivery obligations are similar to Union's obligations and that all customers benefit from the overall arrangements made by both Union and direct purchase customers in ensuring that appropriate volumes arrive at delivery points. 183

Schools also noted that Union does not reflect in rates either the load-balancing benefits of system gas enjoyed by direct purchasers or the diversity and security benefits to all customers of the Alliance and Vector arrangements. 184

Schools stated that Union should stop paying the DCC since EGDI had never paid a DCC, and has had no difficulty maintaining supply to its direct purchase customers. 185

Schools argued that rates are set on the basis of real or forecast costs only. Further, Union could not provide any other examples than the DCC of rates being set based on avoided costs. 186

Schools expressed concern about the aggravating effect Union's proposal would have on revenue to cost ratios. Arguing that these should ratios should be close to 1.0, Schools cited the case of EGDI where large industrial classes have a revenue to cost ratio of 1.03 and the residential class has a revenue to cost ratio of 0.99. Describing a revenue to cost ratio of 0.90 as "already seriously out of balance," Schools stated that "... the current proposals are, even by [Union's] standards, grossly excessive." 187

Schools questioned the meaning of "obligated deliveries," noting that at the advent of gas deregulation in 1986, most direct purchase transactions were at Empress where Union either bought or took delivery of gas and transported it to Ontario via TCPL capacity held by Union. The only direct 188 purchasers who had any latitude with respect to delivery point were the Ontario buy/sells or Ontario bundled-T customers who held upstream transportation capacity, most of whom would have held TCPL capacity and would therefore have had to comply with TCPL's delivery point rules : these were few in number since they would have to accept the risk of holding TCPL FT capacity. Schools noted that most, if not all, of TCPL's FT to the eastern zone was delivered to Parkway.

189

Schools joined VECC and LPMA in dismissing Union's load loss concerns with respect to the VECC proposal, noting the overall bill impacts, Union's ability to negotiate rates, and the possibility of using contract class deferral credits to mitigate any rate impacts.

190

Finally, Schools criticized Union's proposal as being unfair to M2 direct purchasers in that these customers, unlike M7 and T1 customers, would be worse off after the DCC elimination. Schools remarked on the heterogeneity of the M2 class, noting that it included institutional and commercial buildings, many of whom had been direct purchasers for years: the "misfortune" of school boards, building owners, and the like who direct purchase sizeable volumes, to be in the M2 class stemmed from Union's restrictions regarding the aggregation of buildings under common ownership for ratemaking purposes. As an example, Schools stated that under Union's proposal, the average school in Union's franchise area would lose a DCC payment of $582 and gain a delivery rate reduction of $127.

191

Schools supported VECC's proposal. Schools did not advocate separate compensation for M2 direct purchasers. However, if the Board accepts Union's proposal, Schools argued it must be modified to treat all direct purchasers equally.

192

CAC argued that the Board had to resolve four issues: (i) whether Union's "DCC-equivalent" rate proposal should be viewed as compensation for a system benefit provided by direct purchasers or as an incentive to retain direct purchasers' loads; (ii) whether Union has provided sufficient justification for its proposal; (iii) whether rejection of Union's proposal would be fair; and (iv) the appropriate mitigation should Union's proposal be rejected.

193

CAC disputed Union's interpretation of the DCC as reflecting a system benefit, noting that the Board had never reviewed the question of whether obligated deliveries provided a benefit that should be paid by system customers: the Board's acceptance of settlement agreements in which the system benefit rationale was made does not constitute a thorough review of the ratemaking principles embodied in the DCC proposal.

194

CAC disputed Union's characterization of the Board's EBRO 412-I Decision that Union could not unilaterally impose a delivery point for fear of inhibiting the development of a competitive Ontario commodity market. CAC argued that Union's position views the preservation of the historic rationale of the DCC as the fundamental issue, ignoring the facts that the competitive market is fully developed and that utilities and their direct purchase customers have far more contractual freedom today.

195

CAC stated that prior to DP, all customers were system customers, contributing to optimal system operation. The development of DP meant that Union could not control whether deliveries would be made as required. CAC interpeted the DCC as a payment to direct purchasers to control the risk of failure of DPs to honour their obligations to deliver and hence incent system optimization. CAC noted however that optimal system operation benefitted direct purchasers and that "[t]he anomalous result ...

was that Union's system customers had to pay DP customers to do not only what was in their interest, but what was a matter of contractual obligation."

196

CAC submitted that the DP customer's obligation to deliver is no different than obligation they had as system customers and that all customers benefit from delivery of required volumes at required locations. Therefore, no inter-class payment is required.

197

CAC argued that rate shock concerns are properly addressed by mitigation measures; they are not a proper rationale for Union's rates proposal.

198

CAC argued that Union had failed to justify the basic elements of its proposal, i.e., that DP customers provide a benefit for which they deserve to be compensated, that DP customers would not honour delivery obligations without a DCC-equivalent allocation, that the DCC calculation is reasonable, and that without the DCC-equivalent allocation there would be significant fuel switching.

199

CAC agreed with VECC and others that Union's proposal, through allocating costs that have not been incurred, violated cost causality principles.

200

CAC argued that parties' expectations of DCC or DCC-equivalent payments do not constitute a basis for ratemaking in the absence of a sound economic rationale. CAC acknowledged that while avoiding rate shock was an important regulatory principle, it did not provide a basis for accepting Union's proposal but, rather, argued for rate mitigation measures. In rejecting Union's proposal, CAC accepted the need to eliminate the DCC but proposed a five-year phase out of the plan to mitigate potential adverse effects.

201

Kitchener noted that Union has always depended on obligated Parkway deliveries and, prior to 1987, had no concerns in this respect because Union arranged all deliveries to its system. Kitchener acknowledged that in the early days of DP, an obligated delivery premium was necessary to increase the competitiveness of the gas supply market. However, Kitchener argued that the need for this incentive has disappeared due to the EBRO 456-4 Decision in which the Board allowed Union to mandate obligated deliveries. The maturity of DP makes cross-subsidization by system gas customers unnecessary, and undesirable.

202

Kitchener noted that the avoided cost rationale for the DCC, which gave rise to cross-subsidization, was proposed by Union on an interim basis in EBRO 494-06, with the Board accepting it as such while contemplating a full review in the next main rates case. Kitchener submitted that there has never been a full Board inquiry into the cost implications of the DCC methodology; in fact, "... the cross-subsidization ... was never revealed until RP-2001-0029."

203

Kitchener claimed that Union's proposal was not in compliance with the Act's requirement that rates be just and reasonable (s.36(2)) insofar as the proposal violated cost causality principles by requiring system customers to bear the cost of the reliability concerns caused by DP's actions. Also, the proposal results in revenue to cost ratios significantly at variance with the ratios last approved by the Board in EBRO 499. In this latter regard, Kitchener argued that "... the Board's approval of a utility's rate design in any case is essentially an approval of the resulting revenue to cost ratios. ... Having approved in EBRO 499 the rate design ... the Board should not depart from that approval during the PBR term, absent extraordinary circumstances."

204

Kitchener maintained that Union's approach of allocating avoided, not actual, costs was both dangerous, due to the introduction of cross-subsidization, and unprecedented, since the approach is not applied to any other avoided costs or system benefits, such as Union's Alliance and Vector arrangements. Kitchener stated that "... in an integrated system like Union's, each customer class benefits from the presence of the other customer classes and these interrelated benefits are not accounted for by cross-subsidization." Further, Kitchener argued that the need for the DCC is obviated by the existence of contractual obligations and penalties.

205

Kitchener noted that firm deliveries for system customers do not receive a DCC credit while firm Dawn deliveries -- which entail no avoided cost benefits -- receive the DCC credit. Kitchener added that "the customer classes which bear the burden of Union's proposal in this case (M2, M9 and M10) are the same classes who were targeted by Union's flexibility and service basket design proposals in RP-1999-0017 which was rejected by the Board."

206

Kitchener echoed other intervenors in noting that the rate impacts in Union's evidence are delivery rate impacts only and do not account for the commodity and transportation costs of energy supply. Kitchener concluded that the absence of any phasing out proposal from Union indicated that Union was "not unduly concerned about the impact of the intervenor's proposal on its industrial customers."

207

Kitchener urged the Board to eliminate the DCC as per VECC's proposal and consistent with the EBRO 499 approved rate design and with the RP-1999-0017 settlement agreement.

208

IGUA supported Union's DCC proposal on the basis that the avoided cost benefit was an appropriate compensation to direct purchasers for the contractual risks and commitments they have assumed in firm obligated deliveries to a specific delivery point. IGUA urged that if the Board rejects Union's proposal, the DCC not be eliminated.

209

IGUA submitted that prior to direct purchase, Union arranged supply for all its distribution customers by holding a portfolio of gas supply contracts which required delivery at specific points. A "substantial component" of the portfolio comprised firm service contracts requiring TCPL to deliver gas to Parkway east end at a 100% load factor. IGUA added that the Board and intervenors accepted "at all material times" that these deliveries benefitted the system through reduced Dawn-Trafalgar facility requirements, the avoided cost of which was a reasonable measure of benefits and reflected in distribution rates. Further, there would be no cost consequences of a delivery failure for system gas customers if Union did not suffer a loss or if Union did suffer the loss but the Board did not approve cost recovery.

210

IGUA argued that this was in contrast to the predetermined cost consequences including DCC clawback and automatic penalties, spelled out in the contract, for a direct purchaser's failure to deliver. IGUA added that direct purchasers, unlike system gas customers, derive no benefit from Union's "diversity as system supplier."

211

IGUA submitted that the introduction of direct purchase resulted in the replacement of suppliers' contractual commitments to Union with direct purchasers' contractual commitments to Union, enabling continued system benefits in the form of avoided facilities' costs. IGUA admitted that while the calculation of this benefit had changed, "... the entitlement of direct purchasers to receive that consideration has remained constant." IGUA maintained that this consideration was justified due to the assumption by direct purchasers of the risks of obligated Parkway deliveries.

212

IGUA argued that the evidence showed that direct purchasers' contractual obligations were more onerous than those of system gas customers and, therefore, by VECC's argument, were entitled to consideration -- either as a credit on their bill or as a rate reduction--for being relatively disadvantaged.

213

IGUA described Union's evidence as revenue neutral and consistent with the status quo whereas VECC's evidence was not revenue neutral and would radically alter the status quo. Accordingly, IGUA submitted that the onus was on VECC to make a convincing case.

214

IGUA argued that VECC's position ignored the impact of its proposal on individual distribution bills, with some large volume users to see an increase of more than $1 million annually for distribution services. Based on the resulting increases VECC's proposal would entail for rates M5, M6, M7, and T1, IGUA submitted that VECC's proposal was not revenue neutral; on the contrary, because the net distribution bills for contract customers would be almost unchanged under Union's proposal, IGUA submitted that the utility's approach was revenue neutral.

215

Denying VECC's claim that the delivery obligations [on behalf] of system customers were similar to those of direct purchasers, IGUA submitted that Union acted as a principal, not as an agent, in contracting for system gas: system gas customers had no contractual responsibilities for delivery to Union. IGUA asserted that there was no agency relationship between Union and its system gas customers. Also, since direct purchasers make delivery commitments for the transfer of the custody of the gas at a specific delivery point, and the system benefits through avoided facilities' costs, the volatility of commodity prices was irrelevant with respect to the justness and reasonableness of delivery rates.

216

IGUA disputed the notion that the DCC was a load retention incentive, stating that although load loss must be considered under VECC's proposal due to its "serious negative distribution bill impacts," customers contemplating direct purchase are not threatening to leave the distribution system.

217

IGUA argued that as customers migrate to direct purchase, Union's risks associated with 100% load factor Parkway deliveries would decrease. But, even if all customers opt for direct purchase, while the diversity benefit of Union's role as a gas purchaser would be lost, there would remain a delivery commitment differential for each class based on the difference between the commodity allocation factor and the Dawn-Trafalgar design day allocation factor for each class.

218

OAPPA supported Union's position that the delivery obligations assumed by direct purchasers resulted in an avoided facilities benefit conferred upon all users that deserved consideration.

219

OAPPA noted the testimony of VECC's witnesses that the FST toll that was previously offered by TCPL was a lower rate to recognize the fewer facilities required in offering this service; similarly, interruptible rates are lower to reflect that, in their absence, costs would be higher to meet design day demand.

220

OAPPA submitted that system customers cannot contractually obligate deliveries since these customers do not handle the gas. OAPPA contrasted this with the daily, firm obligation to deliver, regardless of consumption, of direct purchasers.

221

OAPPA submitted that the delivery rate impacts of VECC’s proposal on direct purchasers are shown by the evidence to be significant; further, they are unjustified, given the continued obligation to deliver. With respect to the argument that delivery rate impacts are dwarfed by commodity price fluctuations, OAPPA stated that this view was misguided since direct purchasers have made supply arrangements based on their own risk tolerances "... that simply do not allow a conclusion such as VECC’s to be made with confidence.” OAPPA stressed that "... delivery arrangements and the attendant costs are key elements of a customer’s natural gas supply portfolio and therefore, a major consideration on their own.”

222

OAPPA noted that the customer letters received by the Board supported Union’s proposal. OAPPA urged the Board to adopt Union’s proposal but, failing that, urged the Board to mitigate the impact of adopting VECC’s proposal by phasing out the DCC over a period of no less than five years.

223

Tractebel supported Union’s proposal arguing that: (i) direct purchasers bear a unique delivery obligation; (ii) direct purchasers provide a system benefit; (iii) the system benefit provided is appropriately reflected in rates; (iv) the system benefits are appropriately measured by avoided costs; (v) there is no rationale for changing the status quo; and (vi) changing the status quo will result in rate shock.

224

Tractebel argued that the DP delivery obligations were different and more onerous than either the obligations of system gas customers or the obligations of Union. Tractebel noted that system gas customers are under no obligation to deliver on an even daily basis or to a specific delivery point; nor are system customers liable for failure to deliver. Tractebel submitted that Union "meets the supply demands of its system as it wishes,” citing Union’s use of its northern TCPL capacity to serve the southern area during non-peak conditions. Further, Union does not have to deliver gas that system customers do not consume, nor does Union suffer penalties for failure to deliver.

225

Tractebel noted that all parties accepted that obligated deliveries provided a system benefit. Tractebel stated that this benefit is appropriately reflected in rates because, in EBRO 412-III, the Board approved a premium payment for obligated deliveries to a fixed delivery point in recognition of the system benefit provided. Again, in EBRO 493-04/494-06, the Board accepted the avoided facilities’ cost as an appropriate measure of system benefits. Tractebel argued that the NEB’s treatment of TCPL’s FST rate also recognized avoided costs.

226

Tractebel described Union’s proposal as a necessary modification of the DCC to accommodate unbundling that maintains the underlying DCC principle while VECC’s proposal would "... completely eliminate the principle of paying a premium to customers who obligate their deliveries. ... VECC is saying that the cost allocation associated with the DCC is incorrect, and always has been.”

227

Tractebel criticized VECC’s proposal as ignoring all of the Board’s case law on DCC, remarking that the Board approved different rates for obligated and unobligated deliveries back in EBRO 412-III in 1988. Tractebel argued that although the DCC had undergone modifications as the gas market evolved, the principle and practise of recognizing the system benefits of obligated deliveries had been maintained.

228
Tractebel disputed VECC's interpretation of the issue as a cost allocation issue, submitting that "...[Union's DCC proposal] is best characterized as a rate design issue." Tractebel distinguished between "costs" incorporated in a revenue requirement and "costs" relevant to rate design stating that the former were payment obligations related to operating expenses and capital costs, "direct costs" defined by Tractebel, while the latter, as per Bonbright, was a broader concept incorporating considerations such as cost causality, avoided costs, and cost shifting.

229
Tractebel dismissed the commodity price volatility argument as bordering on the absurd and urged the Board to approve Union's proposal in view of the delivery rate shock attributes of the competing proposals.

230
Energy Probe ("EP") described the DCC as "a muddle of contradictions" containing both favourable and unfavourable characteristics.

231
EP credited the DCC as providing system planning and control benefits and argued that Union's proposal would strengthen the enforcement of delivery obligations through increased penalties for non-compliance. EP asked the Board to urge all parties to try to increase the liquidity at Parkway to obviate the need for failure-to-deliver penalties in the future.

232
EP argued that historically, the DCC had not been consistently associated with system benefits stating that "[a]t one time, the DCC only represented a difference between the buy/sell reference price and WACOG. Only later was DCC used as a system planning tool." As such, EP urged that the Board "... not feel bound to maintain the status quo, but ... take a more principled review of the issue."

233
EP noted that the DCC was unique and suggested that it was so due to its unfavourable characteristics which included violating basic ratemaking principles, overpaying for DCC benefits, violating the Board's RP-2001-0029 directive, and creating customer confusion.

234
EP submitted that the DCC was based on "what-if" phantom costs as opposed to actual costs incurred. EP acknowledged that while avoided costs are useful in determining whether a particular expense is justified, they are not appropriately included in rates as they do not represent real costs incurred. EP noted that Bonbright's first attribute of a sound rate structure is "effectiveness in yielding total revenue requirements.": as the DCC is not included in Union's revenue requirement, it doesn't belong in rates. EP suggested that "nowhere does Bonbright endorse rate recovery of costs a utility does not bear."

235
Noting that it is obligated Parkway deliveries that avoid costs, EP questioned why Union paid 24% of the DCC between January 1 and October 31, 2002, for deliveries at Dawn and Ojibway when these west end deliveries increase the need for facilities. Further, EP claimed that some DP shippers were "double dipping" at the expense of high coincident peak users since the shippers are paid the DCC for Dawn deliveries -- including capacity associated with the delivery point flexibility which also flows benefits to shippers.

236
EP recommended that DCC payments for west end deliveries be eliminated immediately with the other DCC payments eliminated over a five-year period "unless a cost-based alternative capable of ensuring deliveries arrangements that meet Union's system planning needs can be implemented

sooner.” Until this time, EP agreed with VECC that "the Board has the authority to ensure that Direct Purchase deliveries at 100% load factor are obligated.”

EP envisioned such a cost-based alternative as ensuring that "... the deliveries of, or on behalf of, all 237
customers, including DP and system customers, are economically optimal for the overall system.” Such a system would require customers who demand service at the coincident peak to bear costs of meeting that demand and would provide compensation for relieving congestion only if the utility bears a real cost. EP suggested that the compensation be the minimum payment required to ensure the needed supply and that this amount of compensation might be determined through an auction process.

In Union’s reply argument, Union responded to the charge made by some intervenors that Union had 238
not complied with the Board’s directive in RP-2001-0029, Union stated that the Board did not review the merits of its DCC proposal, nor reject its proposal in the RP-2001-0029 Decision with Reasons. Union’s position is that its DCC proposal had been accepted, by all parties and the Board, in settlement agreements in the preceding EBRO 499 and RP-1999-0017 proceedings. When disagreement arose over the interpretation of "revenue neutrality” in the RP-2001-0029 proceeding, the Board accepted Union’s alternative submission: that the DCC not be eliminated. Union submitted that in bringing forward a detailed justification for its original proposal was consistent with the Board’s directive.

Union added that it had not provided a schedule for phasing out the DCC since its proposal did not 239
involve any phasing out.

Union argued that the Board had always maintained that fixed delivery point obligations should be 240
negotiated, not unilaterally imposed. Noting that DP contracts are typically twelve months in duration, Union submitted that "[t]here is no basis in the evidence for the conclusion that direct purchase customers will continue to make these commitments in the absence of consideration.”

With respect to the payments made to DP customers, Union asserted that DCC costs are in rates and 241
have been from the start. Further, intervenors have agreed with, and the Board has approved of, this arrangement.

Union disputed the contention by some intervenors that issues agreed upon in settlement agreements, 242
such as the DCC issue in EBRO 499 and RP-1999-0017, had not been reviewed, arguing that although they had not been litigated, they had been reviewed by the parties prior to the settlement, and by the Board in accepting the settlement. Union argued that settled issues "... are more reliable [than litigated issues] precisely because experienced parties with experienced legal counsel following a thorough discovery process and extensive negotiations, all in a process financed through intervenor cost awards, have all agreed to a resolution of the issue.”

Union disputed LPMA’s argument that M2 customers would pay twice for facilities, once when they 243
are avoided and then again when they are built. Union argued that obligated deliveries provide a $27M benefit regardless since, in the absence of obligated deliveries, new facilities would be required earlier than otherwise: actual facilities constructed would be incremental to the $27M cushion in avoided costs.

244

Union dismissed VECC's concerns that a DP customer might return to system and receive payment even when deliveries were no longer obligated, stating that these impacts would not be material given the stability of DP activity. Union admitted that there had been migration of system and DP customers back and forth but remarked that DP has been relatively stable, accounting for approximately 40% of customers and 80% of volumes for a number of years.

245

Union submitted that while it needs to know where gas is going to be delivered and that most of the gas must be delivered to Parkway, obligated deliveries at Dawn (and Ojibway, Bluewater, etc.) also provide system integrity and operational benefits and avoid costs that would be incurred if they were not made. Union added that a customer obligated to deliver at Parkway would not be paid the DCC for unauthorized deliveries to Dawn. Also, conceding that a customer who is obligated to deliver at Parkway, could deliver at Dawn if he bought an M12 service for transportation from Dawn to Parkway, Union stated that this did not remove the obligation to deliver at Parkway, it just added an M12 cost to get the gas to Parkway.

246

Union disagreed with the reasoning that the rationale for the DCC no longer existed i.e., the prohibition against unilaterally mandating delivery points was unnecessary since the gas market is now competitive, calling it "completely speculative " and embodying "... a view of competition as a static end state with fixed characteristics." Union's position is that competition is "organic", evolving in unforeseeable ways to changing conditions. Union argued that having a competitive market today does not guarantee a competitive market tomorrow: unilateral mandating of delivery points could change the market of the future.

247

Union vehemently denied that the DCC was a subsidy. On the contrary, it is a recognition of the lower costs (than otherwise) due to obligated deliveries. Union disputed that DP customers would cause costs if they refused to obligate deliveries, arguing that such costs would be caused "... by the high demand, low load factor customers who use the system." Union likened high load factor DP customers who hypothetically would refuse to obligate deliveries and hence require additional facilities to be constructed, to a "generous friend" that had previously sheltered you from costs.

248

Union argued that the DCC cost of a $27M rate reduction would not disappear under its proposal: it would only disappear if "the Board abandoned the principle that, despite what impact it may have on the future evolution of competition in Ontario, Union could not unilaterally impose obligated deliveries with no compensation."

249

Union asserted that the allocation of benefits and costs of the DCC were provided in evidence in both the EBRO 499 and the RP-1999-0017 proceedings. Further, all parties were aware that the DCC was paid on obligated deliveries in the EBRO 493/494 proceedings.

250

With respect to the concern about intra-M2 impacts, i.e., that not all M2 customers will be held revenue neutral under Union's proposal, Union argued that rate changes always impact customers in a rate class differently due to differences between the customer's usage and the class average. While the rate class is designed to be as homogeneous as possible, they are not conceived on the basis that all customers in a class are identical in terms of consumption characteristics. Union stated that Schools concern in this regard was not a flaw in Union's proposal but rather something to be addressed in rate redesign, not in a PBR year.

251

3.3 Board Findings

Union proposes to discontinue the payment of a rebate to Direct Purchasers who have met their contractual obligation to deliver firm gas at an agreed upon delivery point on Union's system. It proposes to replace such payments with rate relief for the erstwhile recipients of the payments. This rate adjustment for Direct Purchasers would be based on and equivalent to the quantum of the payments received by them as a class. Under Union's proposal, the rate adjustment which is designed to replace the rebate payments, would, like the payments themselves, be supported by all other rate classes, and allocated on the basis of each rate class's design day reliance on Union's Dawn-Trafalgar transmission system. 252

The Intervenors who reject Union's proposal do so primarily on the basis that, while the DCC rebate payments should be discontinued, there should be no continuing consequential rate relief for Direct Purchasers. They argue that the revenue requirement associated with the DCC payments, which has been allocated substantially to rate classes which do not qualify for such rebates, should end with the elimination of the payments. 253

In addition to the Direct Purchasers who are Intervenors in this proceeding, the Board has received considerable additional input from Direct Purchase customers of Union who are very concerned about the impact the elimination of the DCC payments will have on their costs for gas supply, unless the payments are replaced by equivalent rate relief, according to the Union proposal. 254

The decision to eliminate the DCC arose out of the Alternate Dispute Resolution process in the seminal RP-1999-0017 case. There was an apparent consensus at that time that the DCC should be eliminated on a "revenue neutral" basis. As noted in the RP-2001-0029 Decision, different parties have different recollections as to the meaning of that term for the purpose of DCC elimination. 255

In the RP-2001-0029 case, Union advanced the same proposal that is under consideration in this case. In light of the diversity of views held by the parties, and the potential for significant rate impacts for some customers, the Board deferred its consideration of the matter to the instant case. The Board required Union to develop an alternate proposal which addressed the rate impact issue, and provided for a phasing in of any such impacts over time. Union has not provided any alternate proposal for the Board's consideration in this case. 256

The rationale for, and the structure of, the DCC has evolved very considerably since its first appearance in a Settlement Agreement in the late 1980's. The programme was first named DCC in a Settlement Agreement in connection with a 1990 case, and the current rationale for the costs allocation, of which more will be said later, was developed in connection with a Settlement Agreement in 1998. 257

The programme has always been a creature of the ADR process, and has continuously evolved to find a rationale within contemporaneous market conditions and policy objectives. 258

In this regard, the Board acknowledges that at times over the last two decades, consensus developed respecting the need to provide incentives to Direct Purchasers to participate as genuine market participants in the Transportation and Storage aspects of the gas supply system. The DCC arose in such a context. As the market changed and developed, the rationale for the incentive it represented changed accordingly, culminating in 1998 with a structure providing for a rebate to direct purchasers 259 based on avoided costs associated with system enhancements. This structure was codified in the Settlement Agreement arrived at in EBRO 499. The theory underlying this rationale, which also underlies the current Union proposal, is that but for the compliance of Direct Purchasers with their contractual obligations to deliver, Union would be compelled to expend funds to enhance its gas transmission system. By this reasoning, all customers are obliged to fund the DCC rebates. The revenue requirement associated with the programme assumes that all contracted for deliveries at Trafalgar are unfulfilled, and all rate classes are allocated a share equivalent to that class's reliance on the system as a whole on a design day basis.

260

What the current programme does not take into account is that the market has now developed to the point where Direct Purchasers have other, more sustainable, incentives to participate in the market as independent market participants. Direct Purchasers volunteer to assume responsibilities associated with the delivery of commodity at negotiated delivery points because they believe on the basis of their business judgement that they can procure and deliver the commodity more cheaply than can the system operator.

261

If the decision to engage as a Direct Purchaser is dependent on the continuation of the DCC payment, or the consequential rate reductions proposed by Union following the termination of the programme, the Board would have expected the evidence to say so, and the continuation of the incentive, in whatever form, would need to be assessed on the basis of fundamental rate design principles, and a full re-examination of the appropriateness and scope of the incentive.

262

None of the evidence before the Board supports the proposition that the decision to become a Direct Purchaser is dependent upon the continuation of the incentive in any form, nor is there any evidence before the Board which suggests that Direct Purchasers will migrate to other sources of energy if the incentive is discontinued.

263

Support for the Union proposal seems to derive from two basic propositions: first, that the Direct Purchasers' obligation to deliver to a stipulated point is such a unique contribution to the system as a whole that all system participants should compensate them for it, and second, that no other system participants create anything like the system benefit created by the obligation to deliver.

264

In advancing the first ground, proponents of Union's proposal suggested that the DP requirement to deliver was a 365 day a year obligation. As pointed out earlier, Direct Purchase customers assume that status voluntarily, with a view to their own business objectives. There is no altruism in that choice. Assuming the natural risks associated with that choice does not give rise to an entitlement for compensation. In addition, DP customers do not have an obligation to balance 365 days a year. In fact, their obligation is to balance within 4% once a year. Because the DP customer is not obliged to balance on a daily basis, it is the system as a whole, i.e. ratepayers from all rate classes, who support Union's reasonable efforts to ensure that the system has the requisite daily supply. It is also noteworthy that participation in the DCC programme is not limited to DP customers who deliver at the Eastern terminus of the Union system.

265

The Board considers that the appropriate measure to encourage compliance with contractual obligations is the development of appropriate and effective contractual penalty provisions.

266

In advancing the second proposition, proponents of Union's proposal seem to ignore the fact that the system customers of Union, while not obliged to deliver or use gas pursuant to contract, are subject to a transmission system monopoly. The existence of this captive core of users is at least as important for the optimization of the Union transmission system as any other group of users, including the DP customers.

It is the Board's view that, while the DCC may well have been seen to be a useful tool in encouraging the development of competitive aspects to the gas supply system in the past, it cannot be sustained in the current environment. The Board therefore supports the consensus developed first in the RP-1999-0017 ADR process that the programme should be eliminated. 267

In supporting the consensus for the elimination of the programme, the Board finds that all remnants of the programme should be discontinued, and that Union's proposal to transform it from a direct payment regime to on-going rate relief for DP customers is not appropriate. 268

The Board notes that Union was neither able to identify any other analogous utility that had a like programme, nor was it able to demonstrate that any other aspect of its rates contain avoided costs as a constituent. 269

The Board is concerned that the elimination of the programme in one stroke could unduly disrupt the business planning and budgeting activities of some DP customers. Such customers have developed a reliance on the current rebate structure, and they should be afforded a reasonable opportunity to accommodate a new context that does not include any element of incentives related to their compliance with their contractual obligations to deliver at a negotiated delivery point. Accordingly, the Board will provide for the proportionate phasing out of the DCC programme over a period of five years. Union is directed to develop the rate schedules reflecting this aspect of the Board's Order and to provide the same to Board Staff and Intervenors. 270

4 DELIVERY POINT FLEXIBILITY 271

4.1 Background 272

The Settlement Process leading to the Board's RP-1999-0017 Decision resulted in the parties agreeing 273 to temporarily use 150 MMcf/d of Dawn-Parkway capacity to provide delivery point flexibility to all of Union's in-franchise customers. The revenue foregone by Union arising from this agreement, which would have flowed from the sale of this capacity to M12 customers, was to be recovered from all in-franchise customers. If the arrangement was not to be renewed, it was agreed that customers would again be obligated to deliver at Parkway and Union would not be able to recover any foregone M12 revenue. This arrangement was to end on October 31, 2003 and is referred to subsequently as the present arrangement.

Union further agreed to facilitate individual customer delivery point requests that exceeded the 20% 274 provided by TCPL, if that customer agreed to pay the foregone revenues. Parties acknowledged that customers must pay for any system wide solution negotiated between TCPL and Union. Union agreed to maintain a queue of those interested in delivery point flexibility and to consult with parties on an annual basis.

Union's prefiled evidence in the current proceeding stated that there was no consensus from parties on 275 continuing to provide delivery point flexibility beyond October 31, 2003, the expiry date of the present arrangement. As a result, Union proposed to reduce delivery rates by approximately $450,000 for November and December 2003.

Union expressed the view, in a response to an interrogatory from Kitchener, that the reason a 276 consensus was lacking on the part of customers to renew the present arrangement was because customers were not comfortable that the cost of the service offset the benefits they were achieving.

Kitchener filed evidence proposing the use of a winter peaking service for a period of up to three 277 years to replace the present arrangement. Kitchener stated that it is possible to obtain a firm delivery contract to deliver gas to Parkway on the TCPL system directly when needed, during the winter season, with any party that holds sufficient firm TCPL capacity to Parkway and 'downstream' of Parkway.

Union filed reply evidence with the Board concerning Kitchener's proposal. In this evidence, Union 278 stated that it did not agree with Kitchener that a peaking service would be a more economic solution at the present time for providing delivery point flexibility. Union stated that this was because the cost of the peaking service would be higher than other options currently available to effect delivery point flexibility, as well as much higher than that of the present arrangement. It would also result in Union having excess gas supply, as a peaking service not only affects the point of delivery, but also includes the delivery of the commodity, which would be surplus to Union's needs.

Union noted that Kitchener had entered into a contract to create its own flexibility. Union stated that 279 this meant that Kitchener had done what Union had been saying customers should do all along to meet their flexibility needs, namely acquire a competitive offering in the marketplace.

280

Union characterized Kitchener’s proposal as lacking any particulars as to availability, cost or terms and conditions and also as providing no economic analysis other than what Union saw as vague and unproven references to "favourable economics.”

281

Union concluded that the Board should reject Kitchener’s proposal on several grounds. First, Union noted that Kitchener was the only party making such a request and Kitchener had not determined whether or not any other customers would be interested. Second, Union argued that Kitchener’s proposal would have a much higher cost than the present solution. Finally, Union said that because Kitchener had met its flexibility needs through the third party contract it had entered into, there was no longer any live issue for the Board to resolve.

282

4.2 Positions of the Parties

283

EDGI and Kitchener were the only parties to provide argument on this issue other than the applicant.

284

EDGI expressed agreement with Union’s position that there is no live issue for the Board to resolve. It noted that Kitchener had entered into its own agreement for a winter peaking service, thereby supporting Union’s view that such services are commercial, competitive commodity services, available in the unregulated market to all customers. EDGI also argued that it was untenable for the distribution utility to be used as a conduit for direct purchase customers to access the competitive market, when, by choosing the direct purchase option, such customers have taken on the obligation to arrange for their own gas supply.

285

Kitchener argued that the degree of interest among parties in a program of delivery point flexibility is not disputable as shown by the present arrangement arising out of the RP-1999-0017 proceeding and its own ongoing attempts to obtain Union’s interest in a delivery flexibility program. Kitchener stated that the key to any economic flexibility program that operates during the winter months is the requirement that it be managed by Union in order to achieve system diversity benefits. It further stated that implicit in its proposal is the notion that Union would act for the benefit of its customers, even when the flexibility service did not involve the use of its own assets or otherwise offer benefits to the shareholder.

286

Kitchener argued that Union’s evidence demonstrated a consistent refusal to investigate a peaking service not of its own design. Kitchener stated that, faced with this reality, it had entered into a customer-specific flexibility solution of its own.

287

Kitchener concluded that Union’s attitude towards the Kitchener proposal meant that it would not be in the public interest to direct Union to test Kitchener’s proposal through consultation design and bidding, as Kitchener had originally proposed. Kitchener stressed that the regulator and intervenors must be vigilant to ensure that assets that have been fully costed and paid for in rates are used to serve the customers that have paid for them.

288

Kitchener concluded that it continued to have concerns about assets being used to serve the customers that have paid for them. Kitchener further stated that given the narrowing of the issues under consideration in this Customer Review Process, it would defer its opportunity to express these concerns until the 2004 application.

289

4.3 Board Findings

290

The Board notes that Kitchener was the only party to this proceeding to support this proposal. However, it also notes that in its final argument Kitchener concluded that because of Union's attitude toward its proposal, it would not be in the public interest for the Board to direct Union to test its proposal as it had originally proposed. Accordingly, the Board will not make an order implementing this proposal.

DECISION WITH REASONS

5 AFFILIATE TRANSACTIONS 291

5.1 Background 292

Union was incorporated under the laws of the Province of Ontario by letters patent dated December 19, 1911. Westcoast Energy Inc. ("Westcoast") owns all of the outstanding common shares of Union. 293

In September 2001, Duke Energy Corporation announced plans to expand its position in the North American natural gas marketplace by acquiring Westcoast. That transaction was completed effective March 14, 2002. 294

There was no evidence filed by Union or any of the intervenors on this issue. 295

In October, 2002, IGUA requested that Union produce copies of any existent plans to transfer Union's storage and transportation business to an affiliate. Under a separate interrogatory, IGUA requested a complete list of affiliate transactions between Union's Storage and Transportation ("S&T") group and DEGT, or any of its subsidiaries, since May 2002. 296

Union's response to IGUA's interrogatories was that Union has no plans to transfer in whole or in part its S&T activities or assets to an affiliate, and that the greatest value of the company is obtained through an integrated approach to the operation of the utility. Since May 2002, Union has entered into 7 contracts with Duke Energy Marketing ("DEM"). The pricing for the services was based on the OEB's approved rates. 297

LPMA requested that Union identify the line of reporting of its S&T group within Union and within Duke Energy Gas Transmission ("DEGT"). 298

In response to LPMA's interrogatories, Union stated that its Capacity Management Department determines the amount of storage to be released and has responsibility to market the assets to the market. Union's S&T group has a direct reporting relationship to DEGT Marketing and Capacity Management in Houston and an indirect reporting relationship to Union's Gas Supply Services. The costs associated with Union's S&T group are charged to operations and maintenance and service provided to affiliates is credited to the operations and maintenance accounts. 299

VECC requested that Union confirm whether DEGT carries out any business or provides services in Ontario's competitive natural gas market and whether Union has provided and billed DEGT for any related services. VECC also inquired about the amount of time Union's S&T group spends on marketing the assets of any affiliates and how any service charges are determined. 300

In response to VECC's interrogatories, Union stated that DEGT does not carry out any business or provide service in Ontario's competitive natural gas market. Union also stated that its S&T group has not provided services to DEGT. For 2002, Union's S&T is forecasted to charge one person's time for marketing non-Union assets. The charge is based on Union's fully allocated costs. 301

Board Staff inquired about any changes in accounting policies, procedures and standards made to Union's accounts since its acquisition by the Duke family of companies. 302

In response to Board staff's interrogatories, Union stated that Union continues to retain operational control over the assets released to provide S&T services and under rate orders approved by the Board. Union has not changed any accounting policies, procedures or standards related to the S&T accounts since the Duke Energy Corporation's acquisition. Union stated that it is in compliance with the Affiliate Relationships Code. 303

Union also observed that DEGT is regulated by the Federal Energy Regulatory Commission ("FERC") of the United States and is governed by a FERC affiliate code of conduct, which is similar in purpose to the Affiliate Relationships Code issued by the Board. 304

Union stated that by centralizing and co-ordinating its marketing efforts both FERC-regulated and Ontario-regulated assets will benefit through Operations and Maintenance ("O&M") cost efficiencies and asset value and asset growth over the longer term will be enhanced. Union's Gas Supply Services Department will still be responsible for supply services. 305

Union stated that Union's Vice President of Gas Supply Services is responsible for oversight of both the release of the excess capacity to the market and the approval of contracts. The application for incremental capacity would be through Union's sales representatives. 306

Union has provided a copy of the draft Service Level Agreement and stated that the transfer price for service is the provider's fully loaded cost. 307

Union stated that it has not turned back any TransCanada capacity in 2002. 308

Union represented in an Undertaking that peak storage is usually offered through a public tender ("open season") and exchanges and off-peak loans are not offered through written tenders but rather through verbal offerings to several potential buyers. 309

Union asserted that the broader issue of other affiliate services associated with the Duke acquisition was not on the Issues List. In its view, the matter should be considered in the course of the 2004 rate case. 310

5.2 Union's Argument in Chief 311

Union asserted that there were two issues before the Board in this Customer Review Process. First, the nature of Union's transactions with DEM and, secondly, the effect of the Service Agreement on S&T marketing services between Union and DEGT. 312

Seven transactions involving Union and DEM have been undertaken. Union stated that in each case, the arrangements were preceded by a form of tendering process. In each case DEM was the highest bidder. Union represented that, since each of these sales took place at or above market prices, they were in compliance with section 2.3.1 of the Affiliate Relationships Code (the "Code"). 313

Insofar as the Service Agreement between Union and DEGT respecting storage and transportation services is concerned, Union asserts that the harmonization of Union's S&T marketing function with DEGT raises no issues which have any implications for 2003 rates or 2002 deferral account balances. In Union's view, this arrangement raises no issues within the scope of the trial PBR plan, and no order is sought or required from the Board in respect of it. 314

Union's S&T business involves selling assets in excess of what is needed to meet in-franchise demand. S&T marketing forces are engaged in finding buyers for this released capacity. The margin from these sales are recorded in a deferral account and are shared with ratepayers on a basis in which 25% of such sales go to Union and 75% is for the benefit of ratepayers. 315

DEGT is a distinct corporate entity, and is subject to the FERC code governing the relationships between affiliated companies. The FERC code is similar in purpose and intent to the Board's Affiliate Relationships Code. DEGT is engaged in the business of marketing S&T assets and the assumption by it of Union's S&T marketing function was done to harmonize and centralize S&T sales operations. 316

Union has indicated that the charge under the service agreement will be at the provider's fully allocated cost, which will be less than Union's cost of providing the same marketing services. The revenue received from the sale of S&T assets will be recorded in Union's financial statements, and subject to the usual shareholder/ratepayer split. 317

Union submitted that since transactions were done at or above market value and the services priced at DEGT's fully allocated costs, the transactions are in compliance with section 2.3.3 of the Code. 318

5.3 Positions of the Parties 319

Kitchener had the following concerns: 320

a) whether the seven contracts with DEM tendered, and on what basis; 321

b) whether Union turned back portions of Union's TCPL capacity and replaced it with gas purchased from affiliates at Parkway; 322

c) the level of competition for service with the acquisition of Union by DEGT, and who the T-service customers will be dealing with in terms of applying for storage and transportation; 323

d) the status of and the content of the service level agreements between Union and its affiliates; 324

e) whether the transfer of Union's S&T marketing function to DEGT was consistent with Union's prior statements on the question, and the impact of the time of disclosure. 325

IGUA was concerned as to whether the outsourcing of Union's S&T's marketing functions would affect the quality of service to ratepayers. 326

VECC concurred with Union that a complete review of the affiliate relationships impact on customer rates should be addressed in the 2004 rate case. VECC suggested that there should be a review of the service quality levels that customers are receiving in light of the fact that some functions may no longer reside in Union. 327

Schools was concerned that Union had not followed the Board's criteria for affiliate transactions set out in RP-2001-0032. 328

Schools pointed out that Union did not originally file any evidence on affiliate transactions, and suggested that if it were not for the fact that questions were raised at the Settlement Conference, Union would likely not have filed any evidence on this matter. According to Schools, the evidence filed provided no rationale for the decisions and no assessment of the costs associated with the changes. 329

Schools went on to observe that Union did not file the Services Agreement between Union and DEGT until asked to do so in cross-examination. Notwithstanding the fact that the reorganization became operational in February 2003, only a draft agreement was filed. The draft did not provide any terms, pricing provisions or description of services offered and received, nor did it demonstrate whether the services were to be provided at market rates. Schools' position is that Union's actions reflect a measure of disrespect for the Board and its rules. It asserted that questions remain as to how DEGT personnel, with little knowledge of Union's facilities can provide the same level of service as the Union S&T group. 330

331

CEED was concerned that Union has made significant changes to the provision of storage services in Ontario. CEED suggested that the Board should initiate a process in which issues of competitiveness of storage in Ontario may be thoughtfully considered.

LPMA and WGSPG were concerned with the continued availability of storage assets to meet the 332
in-franchise requirement and with the potential impact on the S&T deferral accounts. LPMA and WGSPG urged the Board to direct Union to bring contemplated changes in the in-franchise storage and transmission requirement to the Board for approval prior to their implementation.

5.4 Union's Reply Argument 333

Union reiterated that there is no impact on 2003 rates or 2002 deferral account balances arising from 334
the affiliate transactions and there is no aspect within the trial PBR Plan that is affected by such transactions.

Union submitted that nothing in the Affiliate Relationships Code requires prior or public disclosure of 335
its business activities and, in particular, of affiliate transactions.

Union pointed out that the Board should, in principle, be cautious about issuing directives with respect 336
to matters that are not before it. Accordingly, in Union's submission, there was no basis whatsoever for any criticism of Union with respect to its treatment of this issue or for any directions from the Board with respect to the 2004 rate case.

5.5 Board Findings 337

The Board is concerned that recently the Applicant indicated to the Board and intervenors that it did 338
not contemplate any transfer of Union's S&T activities to any affiliated party. In the course of this proceeding it emerged that such a transfer had occurred in February of 2003. While the Affiliate Relationships Code does not require the Applicant to provide any prior notification of such business re-arrangement, it would have been appropriate for Union to be more forthcoming with respect to this change, given its previous pronouncements on this subject.

It may be that the harmonization of the S&T marketing activities represents an increase in the 339
efficiency of the operation. The Board has insufficient evidence before it to come to any conclusion on the subject, nor to determine whether the transfer of the function to the affiliated company is at a price higher or lower than that reasonably attributable to the function prior to the migration

With respect to the seven contracts entered into with DEM, the Board observes that Subsection 2.8.2 340
(c) of the Code requires the utility to provide information as to the utility's specific costing and transfer pricing guidelines, tendering procedures and service agreements. Further, if any of the transactions exceeded $100,000, Section 2.8.3 of the Code requires disclosure of the details of the transaction.

The content of business relationships between affiliated companies in the energy business has become 341
a particular interest of regulators in North America over the last several years. In recent decisions, this Board has indicated its intention to ensure that the effect of such relationships is adequately

understood and captured in the ratemaking process. It is often the case that a lack of clarity or disclosure of such arrangements raises more concerns and obstacles than the actual revelation of the arrangements themselves. Simple compliance with applicable Codes is a minimum standard for a regulated entity. Developing an approach to this subject that addresses the reasonable interests and expectations of the parties and the regulator is prudent, especially in light of the fact that it is likely, if not inevitable, that these issues will arise in the context of the 2004 rate case.

6 OTHER ISSUES 342

6.1 Standard Storage Service and Standard Peaking Service Rate Derivation 343

Union's Argument in Chief 344

Union questioned this subject appearing on the Issues List, noting that the Standard Storage Service 345 ("SSS") and Standard Peaking Service ("SPS") rates are applicable to unbundled services, beginning April 1, 2003, for which there are not yet any customers. Further, Union submitted that the rationale underpinning the services and rates were provided in pre-filed evidence in the RP-1999-0017 proceeding and were settled in the subsequent settlement agreement that was accepted by the Board in that case.

Union added that, pursuant to the RP-2001-0029 proceeding, SSS and SPS rates were included in the 346 2001 and 2002 rate orders. The calculation of the rates was provided once in the working papers attached to the 2001 and 2002 draft rate orders and again in this proceeding. Because there were not any customers for these services, Union used the existing, cost-based T1 storage rates to derive SSS and SPS rates rather than using a cost allocation to the U2 class.

Union added that it was not seeking any change in rate design or terms of service for the SSS or SPS 347 services and, since Kitchener had not sought any specific relief in respect of this issue, advised that "... it would appear that no decision or comment is required of the Board."

Intervenors' Positions 348

Kitchener was the only intervenor to make a submission on this issue. It submitted that although a 349 separate rate for these services was provided in a post-ADR document in the RP-2001-0029 proceeding, the derivation of the rates was first provided in this proceeding. Kitchener accepted that Union could not use a cost study to develop these rates because it was impossible to forecast demand for the services.

Kitchener stated that the appropriateness of the SSS and SPS rates could be deferred to the 2004 rates 350 case but argued that "... the Board should be concerned about the determination and the assumptions that underlie both the SSS and SPS rates" and that "... Union needs to consider developing the rate from the ground up, based on costs posited on assumed demand parameters."

Union's Reply Argument 351

Union made no further submissions on this issue. 352

Board Findings 353

The Board notes that under the Act, one of its objectives and responsibilities is to maintain just and 354
reasonable rates for the transmission, distribution, and storage of gas. As such, the Board expects Union to base all of the rates it seeks to impose on customers in 2004 on an appropriate allocation of costs.

6.2 Lines of Business 355

Background 356

In the RP-1999-0017 decision, the Board directed Union to file financial information segregated by 357
line of business and a cost allocation study as a guide for evaluation of the cost responsibility by line of business and by rate class.

Union stated that its processes, systems, tracking and reporting systems are designed to provide 358
information by rate class, and not by line of business. Union suggested that if it generated financial statements using subjective allocation factors, the result may not be sufficient for sound decision making and could lead to misinterpretations. Union stated that this method of generating financial statements is also contrary to the objectives and basic principles of segmented disclosure as described in Section 1701 of the Canadian Institute of Chartered Accountants ("CICA") Handbook.

Union has dedicated resources to investigate splitting the company into two lines of business, namely 359
(i) distribution and (ii) storage and transportation.

Union indicated that it would be difficult to split the Dawn Operations Centre into discrete storage 360
and transportation elements because of the presence of common plant assets and Operations and Maintenance costs.

Union also noted that gas commodity cost is strictly a pass-through item and there is no reason or 361
justification to require reporting gas supply as a distinct line of business.

The parties agreed to deal with the matter in argument . 362

Union's Argument in Chief 363

364 Union filed a status report on December 20, 2002 stating that it had decided not to reorganize along lines of business because the cost will outweigh the benefits. Union indicated that it will conduct a notional line of business study as part of the 2004 rate case and attempt to report actual performance broken down by notional lines of business.

365 Union requested a withdrawal of the line of business directive or clarification from the Board as to what the line of business information is to be used for.

Positions of the Parties 366

367 CEED submitted that Section 36 of the Act recognizes four distinct lines of business for which the Board sets rates. CEED asked for clarification as to how anyone would be misled if Union reported as directed by the Board. CEED also rejected Union's suggestion that the use of allocation to generate financial statements would be contrary to the Board's objectives. CEED stated that a regulator must understand the operations of the regulated entity, and the Board's directive would lead to a better appreciation of Union's activities.

368 CEED was particularly concerned that in the absence of financial information on a line of business basis, revenues from the regulated transportation and distribution operations of the Utility could be used to subsidize its unregulated storage and gas sales business.

369 CEED indicated that delivery service is the only service which customers must purchase from the regulated business. Other services such as storage, billing and metering are, or will be, open to competition. As a result, the cost for each component should be segregated in order for the customers to make well informed decisions in choosing service providers.

370 CEED rejected Union's contention that reporting on lines of business is a management decision. It contended that the Board's unbundling decision necessarily leads to a situation wherein the utility is obliged to discretely report costs on gas sales, storage, transportation and distribution respectively. It also rejected Union's argument that financial statements by lines of business would be prone to misuse and misinterpretation. It contended that Union could prepare notes to financial statements by lines of business to explain that the statements had been prepared for filing with the regulator and not for accounting purposes.

371 CEED rejected Union's argument that such a methodology would run counter to the objective s and basic principles of segmented disclosure in Section 1701 of the CICA Handbook. CEED noted that this Section explicitly states that "Nothing in this section is intended to discourage an enterprise from disclosing additional information specific to that enterprise or to a particular line of business that may contribute to an understanding of the enterprise."

372 CEED also indicated that since the Board's original direction was issued in its RP-1999-0017 Decision dated July 21, 2001, Union has had numerous opportunities to request that the Board reverse its decision, but has not done so.

Board Findings 373

In its RP-1999-0017 Decision with Reasons, Union was directed by the Board to: 374

> " ...file with the Board and in the customer review process information on revenue-to-cost ratios for rate classes, financial information segregated by line of business, and information necessary to effect the earnings sharing mechanism. The Board expects the Company to consult with Board staff to develop the particulars for the presentations for the information." 375

In RP-2001-0029 paragraph 6.164, the Board stated: 376

> "The Board sees a need to clarify and particularize its stated requirements. However, the Board would be assisted by a report first from Union setting out how it intends to comply with the filing requirements identified in RP-1999-0017. Union is directed to prepare and file such a report before the commencement of the oral hearing in the next CRP, RP-2002-0130." 377

The Board noted that Union had not been timely in producing a report to set out how it intends to comply with the filing requirements. 378

The Board will defer the implementation of the directive pending the outcome of the cost allocation study for the 2004 rate case. 379

In confirming the Board's directive to file the financial information segregated by lines of business, it is appropriate to restate the rationale giving rise to it. 380

Of particular interest to the Board is the development of information which reveals in the clearest possible way the cost allocations and structures governing aspects of the Utility's business which may be subject to competition in the near or mid-term from unregulated market entrants, including market entrants which may be affiliated with the Utility. 381

The separation of the Utility's operations between unregulated and regulated activities means that the Board must be in a position to assess the degree of cross-subsidization from the regulated aspects to the unregulated aspects. This assessment is important to enable the Board to determine whether the legitimate public interest and ratepayer interests in the assets used in the regulated businesses are protected, such that the assets are not expropriated by the unregulated business. 382

Not only would such migration of assets without compensation be unfair to the ratepayers who have supported them through rates, but it would also impair fair competition, insofar as new, unaffiliated market participants would be compelled to compete against an entity which has been enriched by such assets. The Board regards the provision of such information in the form requested to be critical in assessing the degree to which a particular business activity undertaken by the Utility may become subject to competition. 383

The Board is not persuaded by the Utility's assertion that the provision of the information requested in the form requested is futile and wasteful of ratepayers' resources. The Board has indicated its flexibility in structuring the directive so as to minimize costs and complication. But the requirement remains, and subject to constructive suggestions from the Utility as to how to fulfill it, it is the Board's expectation that the information required, in the form in which it is required, will be provided in conjunction with the 2004 re-basing application. Union's undertaking to provide a notional reporting by line of business for the 2004 rates case may form the basis for the fulfilment of the Board's directive. The Utility is encouraged to consult with Board Staff as that undertaking is developed in preparation for the 2004 rates case. 384

6.3 Revenue to Cost Ratios 385

Union's Argument in Chief 386

Union submitted that revenue to cost ("R/C") ratios arise as an issue only due to the reduction in R/C ratios below 1.0 of the contract classes when the DCC payments are replaced by equivalent rate reductions. 387

Union argued that there was no material difference between the "net effective R/C ratios" resulting from the rates which included DCC and which were approved as just and reasonable in EBRO 499 on the one hand, and the R/C ratios under its proposal on the other. Union submitted that column (f) of Exhibit B, Tab 9, Schedule 3, showing current net-of-DCC R/C ratios, and column (i) of Exhibit B, Tab 10, Schedule 5, showing R/C ratios after implementation of its proposal, supported this claim: "... in all instances except rate M6A, to the extent the R/C ratio changed, it moves marginally closer to 1.0." 388

Intervenors' Positions 389

VECC stated that revenue to cost ratios should be close to equilibrium as a general principle, with any divergences to be carefully scrutinized and justified. 390

VECC noted that under Union's proposal, the range of revenue to cost ratios would change, from 1.022 to 0.511 in EBRO 499 (see accompanying table), to 1.06 to 0.295. Under VECC's proposal, the range would mirror the existing EBRO 499 range. VECC questioned the validity of Union's proposal primarily on the grounds that no other jurisdiction had incorporated a similar methodology that transferred system benefits from one class to another in its rate design to recognize avoided facilities costs. 391

Describing the process of analyzing an integrated system to find inter-class cost and benefit consequences as "laborious and unrewarding," VECC argued that "[i]f direct purchase customers get a credit for gas deliveries formerly made by Union before Direct Purchase came to be, then it is important that other types of benefits are recognized and similarly rewarded." Referring to the increased benefits to direct purchase customers arising from Union's Alliance and Vector contracts that allowed direct purchasers the benefits of turning back TCPL capacity and purchasing gas in the secondary market-- while not assuming the cost of the Alliance and Vector capacity, VECC asserted that consistency in rate design would require lower system customer rates in recognition. 392

VECC warned that accepting Union's "unique rate design ideas" could encourage "endless creative and theoretical wrangles about who really benefits from different aspects of Union's integrated system design ... divorced from the well-established principles of cost causality ... ." 393

VECC urged the Board not to accept Union's proposal, citing the Board's "historical and continued need to rely on revenue-to-cost ratios to ensure the just and reasonableness of rates", quoting excerpts from the Board's RP-1999-0017 Decision with Reasons, (paras 2.457 - 2.459): 394

> "The Board is also not prepared to accept the argument that there is no need to provide revenue and cost information on a rate class basis. The Board has generally relied on the revenue-to-cost ratio in determining that there is no unfair assignment of cost responsibility among rate classes. Evidence in this proceeding established no other basis upon which to check for cross-subsidization other than to use cost information." 395
>
> "The Board does not accept Union's arguments that "using a cost based measure, such as cross-subsidy is not meaningful in PBR because rates are judged just and reasonable by not being escalated beyond the restrictions approved by the Board" nor that "the approval by the Board of a level of pricing flexibility means that if Union makes rate changes anywhere within the boundaries of the flexibility constraints approved by the Board, then the result will be just and reasonable rates". The Board can not automatically assume that the resulting rates will remain just and reasonable among classes".
>
> "In the Board's view there will be a continuing need to monitor changes in rate relationships to ensure that rates continue to be just and reasonable. The Board therefore directs Union to file with the Board and provide in the customer review process appropriate cost information, including rate class revenue-to-cost impacts."

LPMA submitted that "... the key question related to the revenue-to-cost ratios resulting from Union's proposal to embed the DCC into delivery rates is whether or not those revenue-to-cost ratios are staying at a level that is reasonable." 396

LPMA provided a table summarizing the R/C ratios (for delivery services) for in-franchise customers as approved for 1999, under Union's proposal, and under the intervenors' proposal. This table is reproduced below. 397

398

Description	Rate Class	1999 Approved	Union Proposal	Intervenor Proposal
General Service	M2	1.021	1.067	1.022
Firm comm/ind contract	M4	1.019	0.936	1.021
Interruptible comm/ind contract	M5A	0.818	0.613	0.816
Seasonal comm/ind contract	M6A	0.583	0.365	0.583
Special large volume contract	M7			

Firm		0.886	0.655	0.873
Interruptible and seasonal		0.511	0.270	0.511
Large wholesale service	M9	1.003	1.033	1.004
Small wholesale service	M10	0.614	0.579	0.558
Contract Carriage	T1	0.792	0.499	0.771

399

In comparing the 1999 approved R/C ratios to the R/C ratios under Union's proposal, LPMA noted the "significant increases" to the M2 and the M9 classes and described the increases as "unacceptable and not reasonable." Further, under Union's proposal, the other rate classes "... see significant drops in their revenue-to-cost ratios."

400

LPMA argued that while the approved 1999 revenue-cost-ratios were found to be reasonable by the Board, the significant changes under Union's proposal demonstrate that the ratios would not remain reasonable. In contrast, the table shows that under the intervenors' proposal, revenue-to-cost ratios are maintained close to their existing levels, thereby better attaining Union's stated objective of ensuring that the R/C ratios stay at a reasonable level.

401

LPMA urged the Board to reject Union's proposal because, in incorporating rates adjustments not based on costs which have been actually incurred, moves away from cost-based rates. "Such a change would be a fundamental change in the way rates are set in this province and would result in rates that are neither just nor reasonable."

402

Kitchener argued that R/C ratios illustrate rate design and provide a measure of whether rates are just and reasonable. It submitted that the last rate design and rates based on a full cost allocation study and approved by the Board were those in EBRO 499. Further, Kitchener asserted that mid-term PBR rate design changes are inconsistent with the PBR principle of tying rate changes to the price cap formula.

403

Kitchener noted that the DCC was the only issue in this proceeding that could alter the EBRO 499 approved rate design and, based on a comparison between the EBRO R/C ratios and the R/C ratios under VECC's proposal, urged the Board to accept VECC's DCC proposal.

404

IGUA stated that the R/C issue arises "... because the rate changes Union proposes produce revenue-to-cost ratios below 1.0 for some contract rate classes with a delivery commitment differential credit and revenue-to-cost ratios greater than 1.0 for those rate classes with a delivery commitment differential debit."

405

IGUA urged that if the concern about R/C ratios was a matter of "optics,"a separate line item in the cost study to reflect the "delivery commitment differential" for each rate class would address this concern. IGUA proposed that for each rate class, this differential would reflect the mix of system sales and direct purchase customers in the class and would quantify the net benefits provided or enjoyed by the class due to the 100% load factor delivery commitments made by direct purchasers. IGUA suggested that the differential for each rate class be derived from the avoided carrying costs of incremental Dawn-Trafalgar facilities.

IGUA added that its "line item in the cost study" approach would provide a better alignment of R/C ratios and "... will better reflect the realities of the redistribution of risks and obligations associated with the provision of 100% load factor deliveries at specific points within Union's system which have ensued with the widespread shift to direct purchase and the consequential transfer of delivery commitments from Union's suppliers to direct purchasers." 406

Regardless of whether such a delivery commitment differential line item is added to the cost study, IGUA submitted that direct purchasers remain entitled to consideration for the system benefits that they provide. 407

Board Findings 408

The Board considers that an appropriate cost allocation study respects generally accepted principles of cost causation. In view of the principle that each rate classes should generally be responsible for costs it has caused to be incurred, the Board believes that revenue-to-cost ratios provide information that is useful in the consideration of the justness and reasonableness of proposed rates. In the absence of conflicting considerations, this approach would yield expected revenue-to-cost ratios of 1.0 for each rate class. 409

The Board acknowledges that, in practice, rates may be approved which do not result in revenue-to-cost ratios of 1.0 for each rate class. This may arise due to conflicting criteria considered in the rate design stage of developing a sound rate structure. 410

Notwithstanding the preceding, the Board believes that any proposal which results in the revenue-to-cost ratio for any class moving further away from 1.0 should be carefully scrutinized and justified before being given regulatory approval. The Board does not agree that any such further deviations from a revenue-to-cost ratio of 1.0 present merely a problem with "optics." 411

The Board notes that there is no evidence before it that any other jurisdiction has approved the inclusion of avoided costs of facilities in rates. As a matter of principle, the Board finds that no rate class should be assigned a cost that has not actually been incurred by the utility. Therefore, as the payment of the DCC is phased out by Union, it is appropriate that the cost embedded in rates be phased out, for the purposes of calculating the revenue requirement and the revenue-to-cost ratio. 412

The Board finds that both the revenues and costs used in deriving the revenue-to-cost ratios should reflect expected actual revenues collected and actual costs incurred. To derive these ratios otherwise, increases the opacity of the proposal and decreases the usefulness of the ratio itself. 413

Therefore, the Board accepts the position of some intervenors that, under Union's proposal, some rate classes that already enjoy a revenue-to-cost ratio of significantly less than 1.0, would see a further reduction in revenue-to-cost ratios. Under VECC's proposal, the class revenue-to-cost ratios would remain closer to those approved by the Board in EBRO 499. 414

Since the Board has found elsewhere in this Decision that the DCC be phased out over five years, it is also appropriate that the revenue requirement component corresponding to the DCC cost responsibility also be phased out over the five-year period. Union is therefore directed to amend its 415 rates to reflect the phasing out of the DCC and to provide the corresponding R/C ratios in its fiscal 2004 rates application.

6.4 Deferral Account Disposition 416

There are three categories of deferral accounts, namely, the Gas Supply Accounts, the Storage and Transportation Accounts and Others. 417

As of December 31, 2002, the Gas Supply Accounts balances consists of; 418

i) Firm Supply Purchase Gas Variance Account (179-80) debit balance of $6.885 million; 419

ii) Other Purchased Gas Costs Account (179-68) credit balance of $35.923 million after adjusting for the Unabsorbed Demand Charge of $3.1 million agreed upon by all parties at the Alternate Dispute Resolution ("ADR”) Settlement; and 420

iii) the Southern Operations Area TCPL Tolls and Fuel Account (179-67) and the Northern Operations Area Heating Value Account (179-89) and the TCPL Tolls and Fuel Account (179-100) totalling a net credit balance of $2.259 million. 421

iv) the total for the Gas Supply Accounts amounts to a net credit of $31.297 million. The Storage and Transportation accounts and Other Deferral accounts amounts to a credit of $981,000. The total to be disposed amounts to a credit of $32.278 million. 422

Union proposed the following disposition of the Gas Supply Account balances: 423

a) **Firm Supply Purchase Gas Variance Deferral Account** 424

$6.885 million will be allocated to firm rate classes in the Northern and Eastern Operations Area, and all rate classes in the Southern Operations Area in proportion to system sales volume in 2002. 425

b) **Other Purchased Gas Costs Deferral Account (Credit of $35.923 million)** 426

i) Flexibility - South - Credit of $1.941 million to be assigned directly to the M2 general service rate class. 427

Flexibility - North - Credit of $0.123 million to be assigned directly to the M2 general service rate class. 428

ii) Unabsorbed Demand Charge 429

430

The Board acknowledges that for this case only, the parties agreed that Union should recover $3.1 million of Unabsorbed Demand Charge for 2002 instead of $6.277 million as originally submitted. Unabsorbed Demand Charge will be allocated based on a special allocation factor as detailed in Appendix C of the Alternate Dispute Resolution ("ADR") Settlement Agreement.

iii) Amount Recovered in Rates - South - $8.150 million.. 431

Amount Recovered in Rates - North - $0.217 million will be recovered in proportion to firm 2002 system sales, ABC-T and bundled-T delivery volumes. 432

iv) Inventory Revaluation and Rate Rider - South - Debit of $0.855 million will be allocated to all rate classes in proportion to 2002 system sales volume in the Southern Operations Area. 433

Inventory Revaluation and Rate Rider - North - Debit of $0.274 million will be allocated to rate classes in proportion to firm 2002 system sales volume in the Northern and Eastern Operations Area. 434

c) **Southern Operations Area TCPL Tolls and Fuel Deferral Account** 435

The credit balance of $2.112 million will be allocated to all rate classes in the Southern Operations Area in proportion to 2002 system sales volume. 436

d) **Northern and Eastern Operations Area** 437

i) Heating Value - North 438

The credit balance of $2.073 million will be allocated to the Rate 01 and Rate 10 classes in proportion to firm 2002 system sales, ABC-T and bundled-t delivery volume for those rate classes 439

ii) TCPL Tolls and Fuel Deferral Account 440

The credit balance of $3.147 million of Fuel Deferral account will be allocated to rate classes in proportion to firm 2002 systems sales volumes in Northern and Eastern Operations Area. 441

The debit balance of $5.073 million on Tolls and Fuel Deferral Account will be allocated to all rate classes in the Northern and Eastern Operations Area firm 2002 system sales, ABC-T and bundled-t delivery volume for those rate classes. 442

e) **2002 Storage and Transportation Related Deferral Accounts** 443

i) Transportation and Exchange Services - Credit of $3.714 million 444

C1 and M12 customers and in-franchise customer will receive an allocation based on their proportional share of actual 2002 available Dawn Trafalgar and Ojibway-St. Clair capacity. The amount allocated to the in-franchise customers in the Southern Operations Area is to be allocated among rate classes in proportion to E.B.R.O. 499 design (peak) day demand and the balance allocated to customer in the Northern and Eastern Operations Area is to be allocated among rate classes in proportion to the allocation of 1999 storage demand costs as approved in E.B.R.O. 499. 445

ii) Balancing Services - Debit of $2.118 million 446

The balance will be allocated to in-franchise and ex-franchise customers (including customers in the Northern and Eastern Operations Area) in proportion to the allocation of peak storage as approved in rates. 447

The forecast Load Balancing Account charges that has been credited to Enbridge Consumers Gas in 2002 will be recovered. 448

The balance related to in-franchise customers in the Southern Operations Area is to be allocated among rate classes in proportion to E.B.R.O. 499 design (peak) day demand and the balance related to in-franchise customers in the Northern and Eastern Operations Area be allocated among rate classes in proportion to the allocation to 1999 storage demand costs as approved in E.B.R.O. 499. 449

iii) Short-Term Storage Services - Credit of $11.307 million 450

The balance will be allocated to in-franchise and ex-franchise customers in proportion to the allocation of 1999 storage deliverability. The balance relating to the in-franchise customers in the Southern Operations Area will be allocated to the rate classes in proportion to E.B.R.O. 499 design (peak) day demand and the balance related to in-franchise customers in the Northern and Eastern Operations Area be allocated among rate classes in proportion to the allocation to 1999 storage demand costs as approved in E.B.R.O. 499. 451

iv) Long-Term Peak Storage Services - Credit of $3.874 million, Other Storage and Transportation Services - Credit of $0.199 million and Other Direct Purchase Services - Credit of $0.672 million 452

The balance relating to the in-franchise customers in the Southern Operations Area will be allocated to the rate classes in proportion to E.B.R.O. 499 design (peak) day demand and the balance related to in-franchise customers in the Northern and Eastern Operations Area be allocated among rate classes in proportion to the allocation to 1999 storage demand costs as approved in E.B.R.O. 499. 453

f) **Other Deferral Accounts** 454

i) Direct Purchase Revenue and Payments - Debit of $4.216 million 455

The balance will be allocated to rate classes in the Southern Operations Area in proportion to Dawn-Trafalgar design day demand 456

ii) Lost Revenue Adjustment Mechanism - Debit of $0.582 million 457

The balance will be assigned to the in-franchise customers based on the revenue impact by rate classes as presented in Exhibit B, Tab 4, Schedule 3 of the Applicant's prefiled evidence 458

iii) Incremental Unbundling Costs - Debit of $3.202 million 459

The balance will be allocated to the in-franchise rate classes in proportion to the 1999 weighted average number of customers for second phase cost only. 460

iv) Intra-period WACOG - Debit of $6.480 million 461

The balance will be allocated to rate classes in proportion to the allocation of the pass-through items that the intra-period WACOG change relates to. 462

v) Pipeline Integrity - Debit of $2.189 million 463

The balance will be allocated to rate classes in proportion to 1999 total other transmission demand related costs in the Southern Operations Area and in proportion to 1999 total distribution related costs in the Northern and Eastern Operations Area. 464

There was a complete settlement on all components of the deferral accounts and the disposition of the balances. 465

The Board acknowledges that the agreement is without prejudice to the position of any party in any future proceeding in which the entitlement to recover UDC incurred in prior years or on a forecast basis and/or the manner of its recovery from ratepayers are raised as issues. 466

7 IMPLEMENTATION AND COST AWARDS 467

7.1 Rate Implementation 468

Background 469

Union proposed to combine the cumulative 2003 delivery and gas supply transportation rate adjustments and the 2002 delivery and gas supply transportation related deferral accounts balances and refund the total as a one-time credit based on 2002 consumption after July 1, 2003. This delay is to avoid confusion with the payment customers are making in respect of the cumulative impact resulting from the RP-2001-0029 proceeding. 470

Union proposed to dispose of the 2002 gas supply commodity-related deferral accounts balances based on the 2002 systems sales volume. The timing will coincide with the 2003 delivery and gas supply transportation (Northern and Eastern Operations area) rate adjustments and 2002 delivery and gas supply transportation-related deferral accounts disposition. 471

The Board has previously approved Union's proposal to recover the cumulative impact of 2000, 2001 and 2002 delivery and gas supply transportation (Northern and Eastern Operations area) rate adjustments and 1999, 2000 and 2001 delivery and gas supply transportation-related deferral accounts balances over the six month period from January 1, 2003 to June 30, 2003. 472

Union proposes to implement delivery and gas supply transportation (Northern and Eastern Operations area) rate changes for 2003, effective January 1, 2003 on or around July 1, 2003 provided that Union receives the Board's Decision in this case early in May 2003. 473

Positions of the Parties 474

VECC proposed that Union dispose of the balances in the deferral accounts within 60 days from the time the decision is given instead of July 1, 2003 as Union has proposed. 475

VECC's view is that the one-time credit method of refunding the balance would not confuse customers as to the nature of the credit if it was represented on a separate line item on the bill. 476

VECC felt that the one-time credit will provide assistance to low income residential customers who have been burdened with the 2000-2002 adjustments. 477

Board Findings 478

The Board acknowledges that the one-time credit will provide assistance to low income residential customers. 479

The Board is concerned that customers may still be confused about the nature of the credit as opposed to the debit adjustment that they have been paying from January to June 2003, arising from the RP-2001-0029 Decision. 480

The Board accepts Union's proposal to dispose the balances on July 1, 2003 or 60 days after the Decision is published whichever is later. Since the final arguments were not received until March 14, 2003 and given that 60 days lead time is required prior to implementing the disposition, it is the Board's view that July 1, 2003 is a reasonable date for disposition of the deferral accounts balances. The Board directs Union to provide a draft rate order and supporting schedules incorporating the Board's Findings in this Decision. 481

7.2 Cost Awards 482

The Board received cost submissions from the following parties: 483

484

GEC

CAC

LPMA

WGSPG

IGUA

VECC

OAPPA

Pollution Probe

Energy Probe

CEED

OASBO

CME

By letter dated May 5, 2003 Union filed objections to the cost claims submitted by CEED, IGUA and VECC stating that some hours claimed were in respect of the Market Hub Partners proceeding (RP-2000-0139/EB-2002-0415/EB-2002-0421) not the Union proceeding. 485

The Board has carefully reviewed all of the submissions, including the supporting documentation filed with the Board. 486

The Board was greatly assisted by the contributions of the parties and awards all intervenors 100% of their reasonably incurred costs in connection with this proceeding, subject to assessment by the Board's Cost Assessment Officer. The Board directs the Cost Assessment Officer to review the cost 487 submissions of CEED, IGUA and VECC with respect to the objections filed by Union and to make adjustments as necessary. The Board further directs the Cost Assessment Officer to review all cost submissions to ensure they are consistent with the Board's Tariff.

The Board orders that the eligible costs of intervenors, as assessed by the Cost Assessment Officer, 488
shall be paid by Union upon receipt of the Board's Cost Order.

The Board's costs of and incidental to the proceeding shall be paid by Union upon receipt of the 489
Board's invoice.

DATED at Toronto, May 8, 2003 490

Paul B. Sommerville
Presiding Member

Fred Peters
Member

DECISION WITH REASONS

A The Settlement Agreement 491

This document is not available electronically. The document is available in the OEB Public File 492 Room.

B Abbreviations Used in RP-2002-0130 493

Abbreviations used in RP-2002-0130 494

495

Act	the Ontario Energy Board Act, 1998, S.O. 1998, c. 15, Sched. B
ADR	alternative dispute resolution
Alliance	Alliance Pipelines
Alliance Vector	the Alliance and Vector pipelines
Application	Union application dated May 22, 2002
Board	Ontario Energy Board
CAC	Consumers' Association of Canada
Kitchener	The Corporation of the City of Kitchener
CEED	Coalition for Efficient Energy Distribution
CICA	Canadian Institute of Chartered Accountant
CME	Canadian Manufacturers & Exporters Inc.
Conference	the settlement conference in RP-2002-0130
CRP	customer review process of Union's PBR, initially described in RP-1999-0017
DP	Direct purchase
D-T	Dawn-Trafalgar
DCC	the Delivery Commitment Credit offered to Union's direct purchase customers which obligate to deliver to Union at a constant daily rate
DEGT	Duke Energy Gas Transmission
DEM	Direct Energy Marketing
Direct Energy	Direct Energy Marketing Limited
EBRO	Energy Board Rate Order
EGDI	Enbridge Gas Distribution Inc., formerly The Consumers' Gas Company Ltd.
ERF	electronic regulatory filing
FERC	the Federal Energy Regulatory Commission, USA
FT	firm transportation
FST	firm service tendered

GEC	Green Energy Coalition
GJ/d	Gigajoules per day
HONI	Hydro One Networks Inc.
HVAC	The Heating, Ventilation, Air Conditioning Contractors Coalition Inc.
I	inflation factor based on GDPPI
IGUA	Industrial Gas Users Association
IR	interrogatory
Kitchener	The Corporation of the City of Kitchener
LDC	local distribution company
LPMA	London Property Management Association
MMcf/d	million cubic feet per day
NEB	the National Energy Board, Canada
NRRI	the National Regulatory Research Institute, USA
NOVA	Nova Chemicals Corp.
OAPPA	Ontario Association of Physical Plant Administrators
OEB	Ontario Energy Board
PBR	performance based regulation
PCI	price cap index
PGVA	purchased gas variance account
RP-1999-0017	proceeding to hear the application dated March 5, 1999; see decision dated July 21, 2001
RP-2001-0029	proceeding to hear the Application dated July 30, 2001, this application
Schools	Ontario Association of School Business Officials
Settlement Agreement	RP-2002-0130 Settlement Agreement approved on February 17, 2003
S&T	Storage and Transportation
SSS	Standard Storage Service
SPS	Standard Peaking Service
Stelco	Steel Company
TCPL	TransCanada PipeLines Limited
Tractebel	Tractebel
Union	Union Gas Limited

VECC	Vulnerable Energy Consumers' Coalition
Vector	Vector Pipelines
WACOG	weighted average cost of gas
WGPSG	Wholesale Gas Purchasers Service Group
X	productivity and input price index factor