

**REPLY EVIDENCE OF
THE ASSOCIATION OF POWER PRODUCERS OF ONTARIO
NATURAL GAS ELECTRICITY INTERFACE REVIEW**

BOARD FILE NO. EB-2005-0551

MAY 26, 2006

The Association of Power Producers of Ontario (APPrO) is submitting Reply Evidence on two issues: (1) the Obligated DCQ requirement for Union Gas T1 customers and (2) gas utility market power, particularly as it relates to the pricing of storage services to in-franchise customers. The first issue is related to Proposal 8 in APPrO's prefiled evidence, and responds to supplemental evidence filed by Union Gas on May 1. The second issue is related to evidence filed by Union Gas and others in Issue II of this proceeding, but is closely tied to APPrO's Proposal 3, which concerns the pricing of storage services to in-franchise customers.

1. Obligated DCQ for Union Gas T1 Customers

In its prefiled evidence APPrO explained that the Obligated DCQ feature of the Union Gas T1 rate schedule, which requires customers to deliver gas to Union even when there is no gas being delivered to the customer, is incompatible with the operation of dispatchable gas-fired power generation. APPrO provided an example to show that this requirement can impose a large financial burden on a gas-fired generator.

Coincident with the filing of APPrO's evidence, Union Gas filed supplemental evidence on Issue I which addresses the issue of the Obligated DCQ. Using the hypothetical example of a 500 MW power generator, Union states that eliminating the Obligated DCQ for a customer located east of Dawn would create "a substantial requirement (50,000 GJ/d) for either Dawn to Parkway transmission capacity or for alternate arrangements to serve the peak day requirements that are not met by the obligated DCQ at Parkway".¹ Based on the current M12 tolls, Union suggests that eliminating the Obligated DCQ for

¹ Exhibit A, Tab 3, page 4

this customer would create costs of \$1.5 to \$2.0 million per year that Union Gas would have to recover from its other customers.²

APPrO disagrees with Union's example and the resulting conclusions. To begin with, the example does not accurately describe the APPrO proposal. APPrO's primary concern, as stated in its evidence, is that T1 customers should not be required to deliver gas to the utility on days when the utility is not required to deliver gas to the customer. APPrO is not saying that a T1 customer should have the firm right to receive 100 percent of the customer's peak Contract Demand on days when no gas is being delivered to the utility, or that Union Gas should design and construct transmission facilities to meet such an obligation.

The Union example also appears to be inconsistent with the terms and conditions of the T1 service. Under Paragraph 7.01 of Section 2 of the Terms and Conditions for the T1 service, in the event that a customer is not delivering an Obligated DCQ to Union, Union's obligation to deliver gas to the customer is limited to the sum of:

- "a) the confirmed Nomination quantity of Gas to be delivered to Union;
- b) Alternate Supply Gas if acquired by Union;
- c) Customer's Firm Withdrawal Right...."

Since the example assumes that no gas has been nominated by the customer, and Union does not have a firm obligation to purchase Alternate Supply Gas, the only firm obligation that Union Gas has to transport gas on the Dawn to Parkway system is to deliver the customer's firm storage withdrawals to the point of consumption. This is the only commitment that should enter into Union's decision to construct capacity on the Dawn to Parkway transmission system for this T1 customer, and this obligation is the same whether the customer has an Obligated DCQ or does not have an Obligated DCQ. Eliminating the Obligated DCQ for a customer located east of Dawn would not require Union to construct additional Dawn to Parkway capacity or increase the rates of other Union customers.

Finally, Union's supplemental evidence only speaks to T1 customers with a Parkway delivery point, and does not address the situation of T1 customers whose contracts provide for delivery to Union Gas at Dawn. APPrO understands that Union Gas has already agreed to waive the Obligated DCQ requirement for new customers located west of Dawn. To avoid discrimination between new and existing customers, all existing T1 customers with Dawn

² Exhibit B, Tab 3, page 5

delivery points should be given the option to reduce or eliminate their Obligated DCQ requirements.

2. Treatment of Affiliates in Assessing Market Power

Union Gas and Enbridge have stated that in-franchise customers should be charged market rates for storage services that exceed the customer's base or core requirement for storage. This position is based on the assertion that the Ontario utilities do not have market power in the sale of storage services to these in-franchise customers, at least with respect to the portion of these customers' storage service demand for which the utilities have proposed to charge market rates. To support this assertion, both utilities have referred to the storage market competition study conducted by Energy and Environmental Analysis Inc.³ The EEA study, in turn, makes extensive reference to Federal Energy Regulatory Commission (FERC) policies for assessing the market power of natural gas pipelines and storage operators under its jurisdiction.

The FERC policy statement on alternatives to cost-of-service ratemaking makes clear that capacity owned by affiliated companies must be included in measuring market share and industry concentration.⁴ EEA considers this type of affiliate relationship in acknowledging that gas storage owned by Union's affiliate Market Hub Partners would need to be included in a concentration analysis for the Ontario storage market.⁵ However, EEA does not directly address the issue of affiliate ownership of both storage and related gas transportation services.

FERC recently dealt with the relationship between storage and transportation in issuing certificates of public convenience and necessity to Wyckoff Gas Storage Company, LLC, one of the market-based rate decisions cited by EEA.⁶ The affiliate concerns in this case stemmed from the fact that, at the time the original certificate was issued, National Fuel Gas Supply Corporation held a two percent non-voting interest in Wyckoff, with an option to acquire a larger ownership stake at a later time. National Fuel is a large owner of natural gas storage in the New York-Pennsylvania market area in which Wyckoff would be located, and also operates interstate and intrastate pipelines in the same market.

³ "Analysis of Competition in Natural Gas Storage Markets", dated April 28, 2006 ("EEA Study").

⁴ "The capacity on pipeline systems owned or controlled by the applicant's affiliates should not be considered among the customer's alternatives. Rather, the capacity of an applicant's affiliates offering the same product are to be included in the market share calculated for the applicant." ["Statement of Policy and Request for Comments" FERC Dockets RM95-6 and RM96-7, January 31, 1996, p. 35]

⁵ EEA Study, p. 53.

⁶ Order Issuing Certificates, FERC Docket CP03-33, et. al., October 5, 2003.

In its order, FERC noted that Wyckoff would connect to multiple interstate pipelines (Tennessee Gas Pipeline, Columbia Gas Transmission and Dominion Transmission), but was not proposing to connect its storage facilities to National Fuel. Wyckoff had argued that because the interconnecting pipelines were all non-affiliates, customers would not be dependent on transportation from an affiliated pipeline in order to receive service from Wyckoff. FERC also stated that National Fuel's two percent non-voting interest was below the 10 percent threshold FERC used to determine affiliate control. Based on these facts, FERC allowed Wyckoff to charge market-based rates. Nonetheless, as it has done in other market-based rate orders, FERC established a number of conditions that would trigger a re-evaluation this authorization at any time:

Wyckoff is advised that its market power and, therefore, its market-based storage rates are subject to re-examination in the event that: (a) Wyckoff adds storage capacity beyond the capacity filed in this proceeding, (b) an affiliate proposes to construct or acquire an interest in another storage field in the New York/Pennsylvania market area, (c) an affiliate links storage facilities to Wyckoff, **(d) Wyckoff or an affiliate acquires an interest in or is acquired by an interstate pipeline connected to Wyckoff, or (e) National Fuel acquires a 10 percent or greater interest in Wyckoff.** (emphasis added)

The relationship between storage and related transportation services must also be addressed in evaluating competition in the Ontario gas storage market. This is especially important for in-franchise customers who do not have readily-available alternatives for transporting gas to their end use location. In the Natural Gas Forum report, the Board emphasized the close relationship between storage and transportation services as it relates to the services required by gas-fired generators:

"...the anticipated rise in demand for storage and for flexible storage services from the new gas-fired generators raises questions related to:

- whether they can access storage at [cost of service] rates in Ontario for any part of their storage needs;
- the pricing of the more flexible storage services that may be needed; and
- the costs and availability of associated transportation, particularly when the associated transportation would require additional investments.

The above points underscore the importance of the availability of non-discriminatory access to the transportation and distribution systems under transparent conditions.”⁷

As long as in-franchise markets do not have access to competitive storage and balancing services that are comparable in quality to the services provided by the utilities, it is unreasonable to require these customers to purchase essential services from their gas utility without the protection of cost-based rates. This is true whether these customers purchase storage services from the utility under bundled, unbundled, or semi-unbundled rate schedules.

⁷ “Natural Gas Regulation in Ontario: A Renewed Policy Framework”, Report on the Ontario Energy Board Natural Gas Forum, March 30, 2005.