

**ONTARIO ENERGY BOARD**

**NATURAL GAS ELECTRICITY INTERFACE REVIEW  
FILE NO. EB-2005-0551**

**TECHNICAL CONFERENCE MAY 16-19, 2006**

**Responses of Mark Stauff to Undertakings  
Given May 18, 2006 on Behalf of Certain Consumer Groups  
("Consumers Undertakings")**

Transcript references are to the transcript of the May 18, 2006 session of the Technical Conference held in the EB-2005-0551 proceeding from May 16-19, 2006.

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Consumers Undertaking No. 1, at Tr. 153:

**"To demonstrate how capacity constraints evidence market power."**

This undertaking arose out of a suggestion by Mr. Leslie that a company that disposes of all of its output through an auction process cannot exercise market power.

By definition a firm has market power if it is able to profitably increase the price of its product above the competitive level for a significant period. The competitive price level will reflect in some fashion the cost of producing the product. Prices above the competitive level could indicate that storage capacity in Ontario is scarce relative to the level that would theoretically be seen under competitive conditions.

That scarcity could exist because Union and/or Enbridge deliberately withhold some available capacity from the market. It might exist because the Utilities have decided not to develop storage facilities that they could have developed economically, while at the same time using their position in the market to prevent or discourage the development of new storage facilities by third parties. It may be that governmental or regulatory restrictions have prevented the development of incremental storage. It is also possible that the geology in Ontario, coupled with the significant risks that would be associated with large sunk investments in storage facilities by third parties, simply make it economically infeasible for third parties to invest in large-scale storage development. How the relative scarcity of storage arose, or is maintained, does not affect the fact that the Utilities are able to maintain the price at a high level now for a portion of the storage in Ontario, and would be able to do so for all of the storage in Ontario if the Board refrained from regulating storage rates generally.

The mechanism that the Utilities elect to use to sell capacity is therefore irrelevant to their ability to exercise market power. If the Utilities' practice was to auction their capacity, they would be able to control the auction price through the setting of reserve or minimum bid prices. No

unregulated party would disable itself from setting a reserve price. If capacity were scarce, for any of the reasons identified above, even an unreserved auction would result in prices above the competitive level. Note that prices will also tend to increase (and also to reflect discrimination amongst customers) if there is a lack of transparency in the market with respect to price and availability of service, i.e. if the Utilities are able to withhold or conceal information concerning the prices paid by other customers or the amount of capacity that is available.

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Consumers Undertaking No. 2, at Tr. 158:

**“To advise whether or not the pipelines in question under FERC have incremental rates or rolled-in rates.”**

Most of the applications by storage operators for market-based rate authority that the FERC has considered involve new storage facilities. Incremental versus rolled-in rate issues only arise in situations where an existing facility is expanded, and the FERC determines that it is appropriate for the customers who contract for the incremental capacity created by the expansion to pay rates that recover all of the incremental costs associated with the expansion. The FERC typically makes such a determination in cases where the effect of the expansion will be to increase rates for existing customers if the costs of the expansion are rolled-in.

In its Rate Design Policy Statement the FERC indicated that it considers that if a company is able to increase its rates by 10% or more, relative to its cost-based rates, it will be able to exercise market power to the detriment of the public interest. None of the FERC cases that Mr. Stauff has reviewed, for the purposes of preparing his testimony or otherwise, involved any issue around whether a potential 10% rate increase is to be measured relative to rolled-in rates for existing customers, or incremental rates, in cases where a pipeline or storage system charges both rolled-in and incremental rates.

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Consumers Undertaking No. 3, at Tr. 177:

**“To produce explanation of calculation/assumptions.”**

The request was for workpapers and/or further detail concerning the calculations set out in Appendix 2 to Mr. Stauff’s filed evidence.

Attached is a revised and supplemented Appendix 2. A review of the originally filed Appendix 2 and Union's U-2 rate schedule indicates that the cost-based rate calculated for Union storage in Appendix 2 is overstated because of the inclusion of charges for incremental injection and withdrawal capacity. The Revised Appendix 2 calculates a Union storage rate of \$0.29/GJ, rather than the \$0.56/GJ set out in the original Appendix 2.

The entire Appendix has been revised to include certain headings to clarify the units used, to provide further detail of the calculations, and to correct minor errors. After each table in the Appendix a "Notes" section has been added that explains the calculations in the table. References to the applicable tariff sheets for the various storage and transportation service providers have also been included.

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Consumers Undertaking No. 4, at Tr. 201:

**“To provide the information as to what those decisions are that you’re referring to that you say you have and you would look at without doing any further research.”**

The discussion between Mr. Stauff and Mr. Cass leading up to the undertaking concerned differences and similarities between the fact situations in CRTC forbearance proceedings and the fact situation in this case. The CRTC cases that Mr. Stauff reviewed prior to preparing his testimony were:

Telecom Decision CRTC 94-19, *Review of Regulatory Framework*  
Telecom Decision CRTC 95-19, *Services provided by Non-Dominant Canadian Carriers*  
Telecom Decision CRTC 98-17, *Regulatory Regime for the Provision of International Telecommunications Services*  
Order CRTC 2000-553, *Forbearance Granted for Telcos' Wide Area Network Services*

Subsequent to the Technical Conference, Mr. Stauff also reviewed the recent Telecom Decision CRTC 2006-15, *Forbearance From the Regulation of Retail Local Exchange Services*.

Mr. Stauff was asked questions concerning the basis for the claim made in his evidence that there are significant factual dissimilarities between CRTC cases and the present case (Tr. 194-197), any similarities he may have discerned between CRTC cases and the present case (Tr. 197), and whether or not the CRTC continues to regulate rates for telecom carriers that the Commission has determined do not have market power (Tr.200).

With respect to the latter question, none of the decisions that Mr. Stauff reviewed appears to involve the Commission deciding to continue with rate regulation of a telecom company notwithstanding a Commission finding that the company lacks market power.

With respect to the issue of the dissimilarities between telecom cases and the present case, Mr. Stauff's basic answer is unchanged from that given in his discussion with Mr. Cass. The factual pattern in cases where forbearance has been approved, or where the Commission has indicated that it will likely approve forbearance applications upon the satisfaction of conditions that appear to be achievable, (e.g. Telecom Decision 2006-15) is that services that are functionally equivalent to the services provided by traditional telecom companies have begun to be provided by new market entrants using new technologies (e.g. "VoIP" local telephone service), new facilities, or other means. These competing services appear to be priced competitively with (i.e. at or below) the price of the regulated service, and it also appears that the number of customers that can be served by the new entrants can be increased with reasonable investments. The result is that the traditional regulated providers have lost, or expect to lose, significant numbers of customers to the new competitors.

None of these market features are present in relation to Ontario storage facilities and services. There is no new and cheaper technology for storing gas, or for delivering gas to Ontario during peak periods. There are no significant new competitors inside Ontario, and the supposed "competitors" that the Ontario utilities have in the storage market are established U.S. storage operators that are at a significant cost disadvantage to the Ontario utilities in serving Ontario customers. There is no reason to believe that new market entrants or established ex-Ontario storage operators have competed significant numbers of customers away from the Ontario utilities, or that the Ontario utilities have suffered any loss of market share or revenue as a result of competition from other providers who are able to price their product below the regulated level. It appears that the cost of the limited available alternatives to utility storage is considerably higher than the regulated prices charged by the Ontario utilities, rather than equal to or lower than the regulated prices, as is the case in the telecom cases.

Mr. Stauff concludes that there are no similarities between the factual circumstances in telecom markets and storage markets, and that no useful factual analogies can be drawn between the two types of markets.

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Consumers Undertaking No. 5, at Tr. 235:

**"To provide complete copy of FERC Policy Statement."**

Attached.