

EB-2001-0441
RP-1999-0017

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

IN THE MATTER OF an Application by Union Gas Limited approving or fixing just and reasonable rates for the unbundling of certain rates charged for the sale, transmission and storage of gas;

AND IN THE MATTER OF an Application by Union Gas Limited for the inclusion of Alliance Pipeline and Vector Pipeline contracts in the portfolio of upstream transportation to be allocated to customers electing direct purchase.

BEFORE: George Dominy
Vice Chair and Presiding Member

Malcolm Jackson
Member

DECISION WITH REASONS

September 6, 2001

1. Background and The Application

- 1.1 Union Gas Limited (“Union”, the “Company” or the “Applicant”) filed with the Ontario Energy Board (“the Board”) an application dated March 5, 1999, for an order or orders approving or fixing just and reasonable rates and other charges for the sale, distribution, transmission and storage of gas in accordance with a performance based regulation (“PBR”) mechanism, commencing January 1, 2000. The application, which was given Board File No. RP-1999-0017, sought an order approving the unbundling of certain rates charged by Union for the sale, distribution, transmission and storage of gas. The application also sought approval for Union’s proposed “vertical slice” methodology to allocate a proportionate share of all of Union’s transportation portfolio underlying its system gas supply to system gas customers on migration to direct purchase.
- 1.2 Since the direct purchase option was introduced, the migration of system customers to direct purchase has involved the allocation to these customers of upstream transportation capacity held by the distribution utility. Until recently, the allocation of such capacity by Union has consisted of firm transportation on TransCanada PipeLines Limited (“TCPL”) transmission system. The Board approved this approach most recently in its EBRO 493/494 Decision issued March 20, 1997.
- 1.3 The Board in its decision in RP-1999-0017 accepted the methodology but expressly did not decide on the prudence of the costs of Union’s contracts on the Alliance Pipeline (“Alliance”) and the Vector Pipeline (“Vector”) in the portfolio of upstream transportation contracts which would be subject to allocation.
- 1.4 By letter dated June 7, 2001, Union informed the Board that it had allocated all of the TCPL capacity underpinning its system supply for the Southern Operations Area (“SOA”). By letter dated June 21, 2001, Union proposed a mechanism to continue the “facilitation of migration to direct purchase” until November 1, 2001, pending release of the Board’s RP-1999-0017 Decision. The Board approved a transitional mechanism on June 28, 2001, by which customers choosing direct purchase were

allocated Empress-to-Parkway exchange arrangements held by Union. Union submitted that it expected these exchanges to be fully allocated to customers migrating to direct purchase arrangements that start prior to November 1, 2001.

- 1.5 On July 21, 2001, the Board issued its RP-1999-0017 Decision With Reasons in which it approved the “vertical slice” methodology but did not make a finding with respect to the most recently acquired upstream transportation components to be included in the portfolio from which the vertical slice was obtained, i.e. the Alliance and Vector contracts.
- 1.6 By application dated August 1, 2001 (“the Application”), Union sought an expedited process to obtain Board approval for the inclusion of the Alliance and Vector contracts in the vertical slice allocated to customers electing direct purchase in the SOA; Union’s Application was given Board File No. EB-2001-0441 (RP-1999-0017). Union stated that it needed an early decision in order to be able to continue to accommodate system customers changing to direct purchase. The Application included an example of the vertical slice that a new unbundled or direct purchase customer in the SOA, having a Daily Contracted Quantity (“DCQ”) of 1000 GJ/d, would receive: based on Union’s forecasted SOA system portfolio at November 2001, the upstream capacity allocated at posted tolls would consist of 485 GJ/d of Alliance-Vector, 333 GJ/d of Panhandle, and 182 GJ/d of Trunkline.
- 1.7 On August 3, 2001, the Board issued its Notice of Written Hearing and Procedural Order No. 1 under file number EB-2001-0441 setting out dates for Union to provide evidence to intervenors of record in RP-1999-0017, and requiring intervenors to file written interrogatories on Union’s evidence, Union to respond to the interrogatories, intervenors to file submissions, and Union to file reply submissions. A subsequent procedural order was issued on August 21, 2001, extending the dates for intervenors to file submissions and for Union to file reply submissions.

2. Union's Evidence

- 2.1 Union submitted that, at November 1, 2001, based on facilitating direct purchase activity, its transportation portfolio for its SOA system customers was forecast to be comprised as follows: 84,405 GJ/d (80.0 Mmcf/d) of Alliance-Vector firm transportation capacity, Dawn delivery; 58,028 GJ/d (54.6 Mmcf/d) of Panhandle Eastern Pipelines ("Panhandle") firm transportation capacity, Ojibway delivery; and 31,652 GJ/d (29.8 Mmcf/d) of Trunkline Gas Company ("Trunkline") firm transportation capacity, Bourbon delivery, together with the Panhandle capacity to transport this gas from Bourbon to the Ojibway delivery point on Union's system.
- 2.2 Union added that its arrangement with Alliance allows Union to ship an additional 13,505 GJ/d (12.8 Mmcf/d) without incurring additional demand charges under the Authorized Overrun Service ("AOS") provisions of the contract. Further, the effect of the energy content of Alliance's gas stream being higher than the average pipeline gas energy content would be to increase the gas received from Alliance by an additional 6,854 GJ/d (6.5 Mmcf/d) giving rise to a total potential capacity on Alliance of 104,764 GJ/d (99.3 Mmcf/d).
- 2.3 Union stated that as the RP-1999-0017 Decision accepted that Union was expected to arrange upstream transportation capacity on behalf of its system supply customers, Union would continue to make arrangements for upstream transportation capacity. Union further noted that marketers and industrial customers do not generally enter into the long-term transportation commitments that the National Energy Board ("NEB") requires to support approval of pipeline projects.
- 2.4 Union submitted that in September 1996, due to an incremental capacity demand of 62,007 GJ/d (58 Mmcf/d) forecasted for the SOA, Union entered the TCPL queue for service commencing November 1998. Although TCPL notified Union in February 1997 that Union would not receive additional TCPL capacity for November 1998, Union remained in the queue hoping to receive additional capacity for 1999 from a proposed

TCPL expansion project; the cancellation of the expansion project and the identification of an additional incremental capacity demand of 84 Mmcf/d for November 1999, led Union to seek alternatives (to TCPL firm capacity) in order to meet its updated forecast incremental capacity demand of 142 Mmcf/d for November 1999.

2.5 Union executed a precedent agreement in November 1997 for 80 Mmcf/d of Alliance capacity starting November 1999 (“the Precedent Agreement”). Union submitted that at the time this agreement was signed, Union estimated that the average delivered cost of the transportation to Dawn would range from \$0.11/GJ below, to \$0.08/GJ above the posted TCPL Eastern Zone tolls; if the value of the AOS and higher energy content related to the Alliance route were considered, Union estimated that the Alliance-Vector route could be up to \$0.11/GJ cheaper than TCPL. In January 2000, Union executed a transportation agreement with Vector Pipelines that included firm capacity equal to the firm Alliance capacity (not including AOS or higher energy content capacity).

2.6 Union argued that the Alliance-Vector arrangements were reasonable at the time they were made for the following reasons: (i) the Alliance route provided a competitive alternative to TCPL in accessing Western Canadian Sedimentary Basin Gas; (ii) the Alliance capacity could be expanded at low cost, therefore putting downward pressure on its tolls; (iii) all other alternatives to TCPL capacity were priced at a premium to TCPL rates; and (iv) there was no TCPL capacity available at the time or guaranteed for the future.

3. Intervenors’ Submissions

3.1 CAC argued that the Board’s reservation with respect to long-term contracting for upstream transportation expressed in the RP-1999-0017 Decision, the capacity costs relative to other alternatives, the interest of Union’s parent company in the pipelines, and evidence filed in the Enbridge Consumers’ Gas (“Enbridge”) proceeding with respect to Alliance-Vector transportation, supported a fuller review by the Board prior

to rendering a decision on the issue of prudence of the arrangements. CAC submitted that, if a full proceeding were held, it would file evidence addressing the impacts of these arrangements on ratepayers. CAC did not support CEED's proposal to exclude Alliance and Vector contracts from the vertical slice, but expressed the concern that it would lead to either the suspension of new direct purchase arrangements or higher costs to system customers. CAC urged the Board to give interim approval to including Alliance and Vector contracts in the vertical slice pending a comprehensive review of the issues.

- 3.2 CEED argued that Union's vertical slice proposal presented in its Application of July 31, 2001, differed significantly from the "original" proposal approved by the Board in RP-1999-0017 in the following respects: the July 31 proposal did not allocate any delivery entitlement not supported by transportation contracts to customers electing direct purchase, whereas the original proposal did; the original proposal excluded Alliance-Vector from the vertical slice, whereas the July 31 proposal sought approval to include Alliance-Vector but did not seek approval of the costs; the original proposal considered a transitional mechanism under which the capacity represented by the Alliance-Vector contracts would be met by other existing sources of supply in order to continue facilitating direct purchase pending review of Alliance-Vector's costs, whereas the July 31 proposal seeks the Board's approval for Union to discontinue facilitating direct purchase if Alliance and Vector are not included in the November 1, 2001, vertical slice. Addressing these differences, CEED submitted that the original proposal "made sense" in these respects: the initial vertical slice would contain components whose costs had been approved and the turn-back rights arising from expiring contracts, paid for by system customers, would be accessible to customers electing direct purchase; transportation contracts should not be included in the vertical slice until the Board has the opportunity to fully review them; and, while the Board is considering whether or not to approve Alliance-Vector for vertical slice inclusion, the initial allocation of upstream transportation components for November 1, 2001, could be based on the existing approved portfolio components, i.e., Panhandle, Trunkline, and the "Dawn Delivery Contract" (this being an Empress-Dawn

exchange contract under which the counter-party delivers 29,520 GJ/d at Dawn).

- 3.3 CEED asserted that the daily volumes of 174,085 GJ/d represented by Union's July 31 proposal were less than Union's SOA system daily volume. Although CEED took the SOA system daily volume to be in excess of 203,605 GJ/d (the sum of the July 31 proposal and the Empress-Dawn exchange capacities), CEED stated its exact magnitude is "difficult, if not impossible, to know from Union's evidence ...". CEED noted that the Empress-Dawn exchange contract would expire on October 31, 2001, at which time Union would, under its proposal, acquire turn-back rights which would allow Union to replace the demand served by the expired exchange capacity by spot gas purchases at Dawn. CEED submitted that the flexibility afforded by these rights - to purchase gas at Dawn that is not tied to upstream capacity - is valuable since spot gas at Dawn is cheaper than gas delivered at Dawn under a transportation contract. CEED, adding that Union's original proposal acknowledged "the availability of turn back rights under the vertical slice as a positive feature of its proposal", argued that the July 31 proposal would result in the value of these turn back rights accruing entirely and inappropriately to Union since the costs of this exchange arrangement had been recovered from system gas customers.
- 3.4 CEED took issue with Union's characterization of the evidence provided in the RP-1999-0017 with respect to the Alliance-Vector contracts as being sufficient to examine the prudence of the arrangements noting that the Board specifically noted in its decision that it had not made a prudence determination in respect of Alliance-Vector. CEED also argued that Union could have sought approval of the cost consequences of Alliance-Vector "at any time over the past eight months" yet had failed to do so. CEED remarked that although Union had not sought approval for an increase in transportation costs since March 1999, Union's interrogatory responses indicated that (i) Union's unit transportation costs had increased by 25% over the period March 1999 to February 2001, (ii) Union's weighted average transportation costs for its system portfolio increased by 36% over the period November 1999 to November 2001, and (iii) there is a

transportation-related debit of \$14.6 million for the year 2001. CEED questioned why Union had not sought recovery of these costs earlier and expressed concern that, although Union appeared to be now seeking approval of these costs, Union had not specifically requested a rate adjustment or a PGVA disposal. CEED submitted that, while these transportation costs reflected historically incurred transportation charges, they did not reflect how the costs of Union's current transportation arrangements compare with alternative arrangements, remarking that Alliance-Vector gas delivered at Dawn costs \$0.83/GJ/d more than Dawn spot gas.

- 3.5 CEED concluded by arguing in favour of a more thorough review of the cost consequences of Alliance-Vector prior to inclusion in the vertical slice. CEED added that Union had not justified any deviation from the original vertical slice proposal and submitted that the composition of the vertical slice for November 1, 2001, should therefore consist of 84,405 GJ/d of Panhandle (Parkway delivery), 36,790 GJ/d of Panhandle (Ojibway delivery), 31,652 GJ/d of Trunkline (Parkway delivery), and 29,520 GJ/d of "Turned-back Exchange Contract" (Dawn delivery).
- 3.6 Direct Energy Marketing Limited and the Ontario Energy Marketers Association urged the Board to render a timely decision in this matter so as not to impede commitments made to new direct purchase customers beginning November 1, 2001.
- 3.7 Ontario Energy Savings Corp. filed a letter of comment urging the Board to seek an expeditious solution that would balance parties' conflicting interests.
- 3.8 IGUA accepted the need for a timely Board decision on the components of the November 1, 2001, vertical slice but argued that, if the Board found the record incomplete with respect to the prudence and cost consequences of Union's Alliance-Vector contracts, then the Board should only give interim approval of the vertical slice. Further, IGUA suggested that Alliance-Vector capacity be excluded from an interim vertical slice pending Board determination of prudence and cost consequence issues.

IGUA's proposed interim vertical slice effective November 1, 2001, would consist of 64.7% Panhandle and 35.3% of Trunkline capacity. In this event, to safeguard the interests of system gas customers pending a prudence determination, IGUA suggested that the Board direct Union to establish a deferral account to capture any Alliance-Vector toll at a premium compared to full toll TCPL contracts.

- 3.9 Should the Board include Alliance-Vector in a vertical slice effective November 1, 2001, IGUA proposed that Union be limited in the amounts it could recover from direct purchaser assignees of Alliance-Vector capacity to full toll TCPL with any Alliance-Vector "premiums" not recovered from these assignees to be captured in a deferral account.
- 3.10 Schools argued that it was not necessary that the Board render a decision with respect to the cost consequences of including Alliance-Vector in the vertical slice prior to August 31, 2001, for Union to begin implementing the vertical slice methodology effective November 1, 2001. Schools suggested that the approach taken in the Settlement Agreement in the recent Enbridge proceeding under docket number RP-2000-0040, to establish a notional deferral account, gather information as to the prudence of Enbridge's transportation arrangements, and provide a basis for examination in Enbridge's next rates case, could be adapted for use in this proceeding. Although Schools expressed the opinion that based on the record in this case, Union's portfolio "would appear to be appropriate", Schools argued that the complexity of the issue required more careful review than is possible under the expedited process adopted and as such proposed that the issue be considered as part of a subsequent consumer review.
- 3.11 VECC submitted that system sales customers had been disadvantaged from the EBRO 493/494 decision onwards by the allocation of lower cost, shorter term TCPL transportation capacity to direct purchase customers, leaving system customers with the burden of the longer term, higher cost Alliance-Vector capacity. Further, VECC argued that the proposal by some parties to exclude Alliance-Vector from the November 1, 2001, vertical slice would amount to giving preferential treatment to direct

purchase customers at the expense of system customers. On the basis of “re-establishing a degree of equity between new direct purchase customers and system supply customers”, VECC urged that Alliance-Vector be included in the November 1, 2001, vertical slice. However, VECC did not accept that Union had met its burden with respect to prudence of the cost consequences flowing from the Alliance-Vector arrangements and, arguing that the Board decision in this proceeding would set a precedent in the Enbridge case and also asserting the conflict of interests with respect to contracting for capacity between Union’s parent and its ratepayers, urged the Board to take “all the time necessary to ensure the issue of prudence is completely examined”. VECC suggested that, should the Board find the Alliance-Vector arrangements to be imprudent as a result of a full examination concluded after November 1, 2001, the Board could remedy any harm to affected customers through the use of credit mechanisms or other tools.

4. Union’s Reply Submissions

- 4.1 Union argued that the current proceeding was sufficient to decide the issues of prudence and cost causation of Alliance-Vector, remarking that in the cases of CEED, IGUA, and VECC (i) none had filed evidence, (ii) none had given any indication of intention to file evidence, (iii) and none had established a need to conduct cross-examination on Union’s evidence. Union submitted that that no intervenor had filed or indicated a desire to file evidence nor had any intervenor insisted upon cross-examination of Union’s witnesses.
- 4.2 Union noted that although VECC and CAC had suggested that the need for an oral proceeding could be evaluated after Union’s interrogatory responses had been received, neither made further representations on this issue. Union added that, in its view, intervenors had been given sufficient opportunity to solicit any required information relevant to the issues and therefore did not have a basis for requesting a “fuller proceeding”.

- 4.3 Union stated that the evidence in this proceeding and the evidence in the RP-1999-0017 proceeding were consistent in that, at the time of contracting to meet forecast demand increases, additional long-term firm TCPL capacity was unavailable and the Alliance-Vector capacity was the only viable alternative.
- 4.4 Union took issue with IGUA's proposal that the premium cost of Alliance-Vector (with respect to TCPL tolls) be recorded in a deferral account, arguing that TCPL tolls would be an inappropriate benchmark, given the evidence that incremental firm TCPL capacity was unavailable at the time the Alliance-Vector arrangements were made, and that there was no basis to record transportation contracts that were at a premium to TCPL while not at the same time recording transportation contracts that were at a discount to TCPL. In this respect, Union stated that the evidence showed that its overall portfolio cost of transportation for the twelve month period beginning November 1, 2001, ($\$0.038/\text{m}^3$) was less than the currently approved TCPL toll ($\$0.043/\text{m}^3$).
- 4.5 Union characterized the suggestion by IGUA that marketers only pay the "benchmark" TCPL tolls for Alliance-Vector while booking the premium in a deferral account as "unworkable because an assignment of capacity must be at the tolls Union pays for the assigned capacity. The upstream pipelines will look to the marketer for the tolls once the capacity is assigned."
- 4.6 Union stated that if there were some question as to the reasonableness of the Alliance-Vector costs, then, rather than approve their recovery on an interim basis, the appropriate course of action would be for the Board to hold a one-day hearing immediately to canvass the issues.
- 4.7 Union also disagreed with proposals that its Alliance-Vector contracting arrangements be reviewed in a manner similar to that approved for review of Enbridge's Alliance-Vector arrangements (which included use of a notional deferral account to book tolls) arguing that the Enbridge disposition was irrelevant to this proceeding because: (i) the disposition of this issue in Enbridge's case was part of a comprehensive settlement

agreement to which Union was not a party in a proceeding in which Union's recovery of Alliance-Vector costs were not an issue; (ii) the Enbridge settlement deferred consideration of the Alliance-Vector contracts, whereas Union has already deferred consideration of the Alliance-Vector issue; (iii) a deferral account treatment involving the use of existing TCPL tolls as a comparator about which to book premiums is inappropriate because there was no TCPL upstream capacity available when the decision was made to contract for Alliance-Vector capacity; and (iv) Enbridge's unbundling proposals did not include the assignment of Alliance-Vector capacity to direct purchase customers.

- 4.8 Union asserted that, contrary to CEED's position, Union's current November 1, 2001, vertical slice proposal was the same as the vertical slice methodology approved in the RP-1999-0017 Decision, remarking that the evidence in that proceeding was that the vertical slice would be redetermined each year based on the system portfolio at November 1 of the year. Union submitted that the current proposal, involving only an update in the vertical slice allocation to reflect the system portfolio at November 1, 2001, is consistent with the approved methodology.
- 4.9 With respect to its SOA system portfolio, Union reiterated that the reasons for the changes from November 1, 2000, to November 1, 2001, were as follows: the remaining firm TCPL capacity was exhausted in facilitating direct purchase earlier in 2001; subsequently, the Empress to Parkway exchanges, approved for use as a transitional mechanism to facilitate continuing migration would be exhausted between August 1, 2001, and November 1, 2001; and the Empress to Dawn exchange (capacity 29,520 GJ/d) would expire on October 31, 2001, and, as the capacity would not be required by Union for its system needs for reasons of declining system and direct purchase demands, would not be renewed. Union stressed that its normalized use per customer has been declining and that it not only has to manage the impact of lower system demands but also lower demands for bundled direct purchase customers through annual resetting of Daily Contract Quantities ("DCQs"), any excess capacity associated with which is returned to Union and absorbed in its system portfolio. To manage the excess capacity, Union has eliminated portfolio components

without fixed transportation components (spot gas purchases) and has chosen not to renew the Empress to Dawn exchange contract. Union argued that the diversity of its portfolio, which included spot purchases and short-term exchange contracts, allowed it to reduce its capacity as demand decreased.

4.10 Union submitted that, for the Board to disallow the cost consequences of its Alliance-Vector arrangements, the Board would have to find that Union was imprudent in its contracting decisions given the circumstances at the time. Union reiterated that, in 1996, it forecasted 1998/1999 incremental system gas demand of 142 Mmcf/d with alternatives available to meet this incremental demand limited to additional TCPL capacity, new pipeline construction to Ontario (TCPL's NEXUS project and Alliance-Vector pipelines), U.S. capacity (Panhandle and Trunkline), secondary market capacity, and daily delivered supply. Union argued that of these, the only viable alternative was Alliance-Vector, the others being either unavailable or uncompetitive for the following reasons:

- TCPL informed Union that there was no incremental TCPL capacity available and that the planned NEXUS expansion project was cancelled, leaving the Alliance-Vector arrangements as the only alternative means to get incremental capacity to move Alberta gas to Dawn;
- At this time, because the landed prices at Dawn for Panhandle and Trunkline supply were \$1.04/GJ/d and \$0.98/GJ/d (respectively) above TCPL landed supply while Alliance supply was forecasted at between \$0.11/GJ/d less to \$0.08/GJ/d more than TCPL, Panhandle and Trunkline were not considered to be viable economically compared to Alliance supply;
- TCPL secondary capacity was trading at between \$1.50/GJ/d to \$2.25/GJ/d as compared to firm TCPL capacity at toll of less than \$1.00/GJ/d; and

- With regard to spot gas at Dawn, although the Alliance-Vector projects have since assisted in the development of this market, Union submitted that, at the time, the market was not mature enough for Union to rely upon it for daily supply, and, further, that landed prices at Dawn for daily delivered supplies were at a premium of \$0.84/GJ/d to \$0.93GJ/d to TCPL delivered supply.

4.11 Union argued that the premiums (with respect to TCPL and prior to construction of Alliance and Vector) of the other alternatives indicated there was insufficient capacity to Ontario and that completion of the Alliance-Vector projects have mitigated this imbalance, lowering the premia with respect to what they would have been in the absence of Alliance-Vector.

4.12 Union added that evidence in RP-1999-0017 indicated that, for the most part, it was the gas distributors, and not the industrial customers or gas marketers, that were willing to contract for long-term capacity; evidence in this proceeding also indicated that the National Energy Board requires long-term contracts for a new pipeline before it will issue a facilities certificate.

4.13 Union took issue with CEED's contention that Union's proposal lessened direct purchase customers flexibility in their transportation portfolios arguing that direct purchasers who received 100% TCPL or Empress/Parkway exchanges could make any alternative transportation arrangements that met delivery point requirements upon expiry of the allocated capacity. Union stated that benefits from the flexibility arising from expiration of upstream transportation contracts flowed to the customer only if the capacity had been assigned to the customer. Union noted that customers migrating to direct purchase in the past have benefitted from the ability to access discounted capacity under Union's TCPL turnback policy, an arrangement between Union and TCPL that permitted Union to decline, upon expiry, up to 49% of its TCPL contracted capacity; this allowed the direct purchase customer to turn back up to 49% of their assigned TCPL capacity. Union stated that the existence of

these capacity turnback benefits were due “in large part” to the Alliance and Vector pipelines.

- 4.14 Furthermore, Union stated that more recent direct purchase customers had not been disadvantaged because they were able to turn back less than 49% of their TCPL capacity arguing that (i) because customers can only turn back capacity relating to contracts that expire after they elect direct purchase, less than 49% could be turned back since some of Union’s capacity had already been turned back to TCPL before they elected direct purchase, and (ii) these customers had already benefitted as system gas customers by Union’s turning back capacity to TCPL.
- 4.15 Union asserted that the principle of flexibility benefits arising from expiry of underlying contracts, i.e., that these benefits accrue to the customers being served by the associated capacity, has been respected under its proposal in this proceeding. Union stated that the reason that flexibility benefits due to the expiry of the Empress/Dawn exchange contract were not available to direct purchase customers was that this capacity was used to serve system demands, not direct purchase demands. This capacity, in contrast to the Empress/Parkway exchange contracts, has not been assigned to direct purchase customers and, as such, no flexibility benefits accrue to direct purchase customers upon its expiry. As system demands had declined, Union has decided not to renew this exchange contract. Union added that the transportation flexibility available to direct purchase customers has been increased by: (i) the requirement of the system portfolio to absorb capacity returned to it by marketers whose customers’ demands have fallen; (ii) the 20% delivery point flexibility approved by the Board in its RP-1999-0017 Decision; (iii) the ability of parties to trade capacity in the secondary market or use Union’s transportation clearinghouse; and (iv) the November 2001 vertical slice being composed of 52% of capacity expiring within one year (as compared to the November 1, 2000, vertical slice with 49% of capacity expiring in two years).
- 4.16 In response to the submissions of Schools, CAC, and VECC that the ownership position of Union’s parent in Alliance and Vector, requires

additional regulatory scrutiny with respect to prudence, Union responded that according to the *Ontario Energy Board Act, 1998* (section 3) and the *Ontario Business Corporations Act* (sections 1(1) - 1(5)) Alliance and Vector are not affiliates of Union because the evidence shows that Westcoast has a 23.6% stake in Alliance and a 30% stake in Vector, less than the ownership stake of 50% prescribed for affiliate status under the legislation. Union added that when Union entered into discussions with Alliance, Westcoast had no stake in Alliance and, when Union signed the precedent agreement with Alliance, Westcoast had 11% ownership of Alliance. After the Alliance agreement had been reached, Union submitted that Vector “was the only viable option for moving gas from Chicago to Dawn.” Union stated that the ownership stakes of its parent were irrelevant to its contracting decisions and that intervenors had sufficient opportunity to canvass this issue both in the RP-1999-0017 proceeding and in the current proceeding.

- 4.17 Union stated that an additional advantage of contracting on Alliance was that additional capacity would become available by addition of compression facilities and, as these were less expensive than adding physical pipe, would result in a decrease in average costs on Alliance, other things equal.
- 4.18 With respect to escalation of the Alliance premium since capacity was contracted for, Union stated that this was mainly due to NEB and FERC approved increases in tolls and an increase in the exchange rate, offset partly by an increase in TCPL tolls. Union contended that these subsequent changes were not relevant to the prudence of the arrangements it made.
- 4.19 Union disputed CEED’s contention that there were “massive” increases in its unit transportation costs stating that its average system transportation costs had increased by approximately 26% over the period November 1, 1998, to November 1, 2001, reflecting the changes in Union’s portfolio. Union admitted that Alliance-Vector costs were higher than other components of its portfolio and added that the addition of this capacity to the system portfolio along with “the streaming of TCPL transportation and

exchanges to direct purchase customers” served to increase the costs to system customers.

4.20 Union took issue with CEED’s reference to a \$14.6 million transportation-related deficit for 2001, stating that this referred only to Alliance-Vector and ignored the transportation-related credit with respect to Panhandle and Trunkline.

4.21 Union concluded by asserting there was sufficient evidence to determine the prudence of its Alliance-Vector arrangements, that there was no need to defer a decision on this matter, and that Union was prudent in contracting for Alliance-Vector capacity.

5. Board Findings

5.1 While the Board to an extent shares the concerns of several intervenors that there has not been a comprehensive review of the evidence that relates to the prudence of Union’s actions in establishing its upstream transportation portfolio, the Board accepts the submissions of the retailers that a timely Board decision is required to maintain the current mechanism for customers to transfer to direct purchase.

5.2 The evidence before the Board indicates that Union’s contracts with Alliance and Vector now comprise almost half of Union’s November 1, 2001, upstream transportation portfolio. Exclusion of these contracts from the portfolio for the purpose of the vertical slice allocation to new direct purchasers would result over time in leaving the remaining system customers with a portfolio consisting only of these contracts which currently, on the basis of the evidence, are the higher cost components of Union’s transportation portfolio. The Board agrees with VECC that such an approach could at least in the short run burden remaining system customers.

5.3 The Board further notes that the structure of Union’s portfolio to a degree results from the rules under which direct purchase has operated over the

past several years, namely the assignment of TCPL firm capacity from Union's transportation portfolio to customers who switched from system supply to direct purchase. More recently the diversity of Union's upstream portfolio has been further reduced through the assignment of exchange capacity as a substitute for TCPL firm capacity as Union's stock of TCPL firm capacity was fully assigned.

- 5.4 Union submitted that at the time it entered into commitments for the Alliance and Vector capacity, it had attempted to obtain TCPL capacity but was unsuccessful because of its position in TCPL's queue for new capacity and subsequently because TCPL had cancelled its NEXUS project to build new capacity. Union submitted that, at that time, the Alliance project provided it with the most cost effective option to secure long term firm service capacity for its portfolio.
- 5.5 In this proceeding CEED filed evidence of Mr. Stauff that it had filed in the Enbridge rates case which asserts that the gas utility should have foreseen the future development of the market, the reducing role of system supply and the likely development of transportation contracting alternatives and therefore it should have recognized the financial risk that Union was taking in entering into long term contracts for upstream transportation.
- 5.6 Other parties indicated that, were the Board to provide an opportunity through an expanded process, they would file evidence to test the prudence of Union's decision to enter into the Alliance and Vector contracts. However, they provided little indication in their submissions of the nature of this evidence or the basis on which they would challenge the prudence of Union's decision.
- 5.7 The Board notes that the Alliance-Vector premium to TCPL now exceeds the upper limit of the forecast range given in Union's original assessment.
- 5.8 The Board recognizes that in all cases of prudence review of past actions there is a potentially false clarity of hindsight and that decisions that in current circumstances may appear to have been rash may well have been

perfectly rational at the time they were taken. In this regard the Board understands Schools' position that a prudency review in this matter may well result in finding that Union's actions were prudent but that, because the issues under consideration were complex, the issue would merit reserving on the decision of prudency and providing for a more careful review through a subsequent customer review process.

- 5.9 In order to balance these conflicting requirements the Board finds that it would be in the public interest to include the Alliance and Vector contracts in the November 2001 vertical slice to be used by Union in assigning upstream transportation to system customers that transfer to direct purchase.
- 5.10 The Board is not making a finding on the prudency of the Alliance and Vector contracts at this time. The Board requires that Union maintain records sufficient to enable the Board to make any necessary adjustments to affected customers to reflect the cost consequences of any subsequent finding of the Board regarding the prudency of these contracts and, hence, the reasonableness of the costs which flow from them. Customers who were system gas customers on or just prior to November 1, 2001, and transfer to direct purchase must, in order to claim compensation or refunds if such is found appropriate by the Board, keep verifiable records of transportation service utilized and costs incurred in respect of capacity assigned to it by Union. The Board further directs that this matter of prudency and cost implications be discussed in Union's customer review process to see if a resolution can be agreed to. Should resolution not be achievable, the Board will hold a limited issues hearing to address this matter.

6. Costs

- 6.1 Parties that seek recovery of costs in respect of this application and proceeding are directed to file their submissions by September 17, 2001.
- 6.2 The Board's costs of and incidental to the proceeding shall also be paid by Union upon receipt of the Board's invoice.

ISSUED at Toronto, September 6, 2001.

G. A. Dominy
Vice-Chair and Presiding Member

Malcolm Jackson
Member