



RP-2003-0203

IN THE MATTER OF the *Ontario Energy Board Act, 1998*,
S.O. 1998, C.15 (Schedule B);

AND IN THE MATTER OF an Application by Enbridge Gas
Distribution Inc. for an order or orders approving or fixing just
and reasonable rates and other charges for the sale, distribu-
tion, transmission and storage of gas commencing October 1,
2004

BEFORE:

Bob Betts
Presiding Member

Paul Sommerville
Member

Pamela Nowina
Member

PARTIAL DECISION WITH REASONS

August 31, 2004

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1 INTRODUCTION 12

1.1 THE APPLICATION 13

Enbridge Gas Distribution Inc. (“EGDI”, “Enbridge”, the “Company” or the “Applicant”) filed an application dated December 17, 2003 with the Ontario Energy Board under section 36 of the *Ontario Energy Board Act, 1998*, for an order or orders approving or fixing just and reasonable rates for the sale, distribution, transmission, and storage of gas for EGDI’s 2005 fiscal year commencing October 1, 2004. The Board assigned file number RP-2003-0203 to the application. 14

The Settlement Conference commenced May 17, 2004 and a Settlement Proposal was filed with the Board on June 17, 2004. 15

The Board held an oral hearing commencing June 16, 2004 on the unsettled issues. On the last day of the hearing, August 3, 2004, the Board heard the Company’s reply argument. 16

1.2 REQUEST FOR EARLY DECISION 17

During the Company’s oral reply argument, the Company requested that the Board issue an early decision by the end of August 2004 on the partially settled rate design issues, specifically Issues 15.1 and 15.2. The Company said that it had committed, in the settlement proposal, to implement the various cost allocation changes for the start of its fiscal period on October 1, 2004. In addition, the prescribed QRAM timelines necessitated filing of the QRAM application and supporting evidence in the first week of September. 18

The Company explained that it would be preferable to begin the fiscal period with the implementation of any rate design changes in order to keep their revenue-neutral effect intact. The Company said that a later implementation date would be cumbersome from an administrative perspective and it would likely cause customer confusion. 19

Pollution Probe also asked the Board to consider an early decision on Issue 10.1, which relates to the proposal for a large boiler market transformation program with the necessary budget, so that the program could potentially be in place for January 1, 2005. Pollution Probe explained that this was a special circumstance, in that a number of customers can benefit from an early decision. 20

The Board indicated that it would endeavour to meet the early decision requests in the month of August 2004. 21

1.3 PARTIAL DECISION

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This Partial Decision with Reasons will deal with the following issues :

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- Issue 15.1 Rate Seasonality
- Issue 15.2 Rate 1 Customer Charge
- Issue 10.1 and 10.2 Demand Side Management - Industrial Boilers
- Issue 5.5 Long-Term System Gas
- Issue 11.2 Class Action Suit Deferral Account (CASDA)

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The Board believes that it is expedient to deal with all of these issues now. The Board will address the remaining issues in its main decision which will be issued in due course.

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1.4 SUBMISSIONS AND EXHIBITS

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

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The Board has considered all of 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.

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2 RATE DESIGN 33

The Board has been asked to consider two issues concerning the Company's rate design. The first is the Company's proposal to remove the rate seasonality feature from its rates and the second is the Company's proposal to increase the customer charge for its residential customers (Rate 1) from \$10 to \$11.25 per month. This increase is revenue neutral within the rate class because it represents a shifting of costs from the variable delivery charge to the fixed monthly charge. 34

2.1 BACKGROUND 35

The Company's proposal is to remove rate seasonality from its delivery charge for all rate classes except Rate 135, a rate which largely serves asphalt plants. Currently, the Company's delivery charges contain a small component that is seasonal in nature. At their inception a number of years ago, seasonal differentials were intended to reflect the incremental cost of delivering gas in the winter months, most notably the cost of storage. This means that there are two different sets of rates for most rate classes. The higher set is for the winter season and the lower set applies to the summer season. Certain of the Company's rate classes do not have seasonal rates because of the nature of the services that underpin those rates. These are Rate 9, the container service, Rate 300, firm transportation service, and Rate 305, interruptible transportation service. Rate 135, seasonal firm service, is unique in that it is designed as a seasonal service for summer load customers. Whatever the outcome of the Company's proposal, the seasonal aspect of Rate 135 will not change. The Company's proposal results from its commitment in the 2004 rates case to review the seasonal differential for all its rate classes. 36

The monthly customer charge is designed to recover a portion of the fixed costs related to serving the customer class. These are the customer-related costs such as meters and pipe, meter-reading costs and customer-related operations and maintenance costs, such as those for the call centre, billing, and credit and collections. For Rate 1 customers, the existing \$10 per month customer charge recovers approximately 50% of these customer-related costs. The Company stated that from a pure rate design perspective, it would be desirable to have a higher proportion of the fixed costs recovered through a fixed charge in order to better match cost causality with cost recovery. The proposed \$11.25 monthly customer charge would recover approximately 60% of the fixed costs of that rate class. The existing \$10 customer charge has been in place since 2000 when it was increased from \$9. 37

2.2 BOARD FINDINGS 38

Rate Seasonality 39

The Company has made a number of arguments in support of its proposal. 40

- The rates would have a simpler rate structure and therefore result in less customer confusion; 41

- The removal of rate seasonality has minimal bill impact; 42
- It is revenue neutral to the utility at the rate class level; 43
- It would bring the Company into alignment with other Canadian gas utilities that do not employ rate seasonality; 44
- The QRAM presentation would be somewhat streamlined; 45
- The role of seasonal rates has been overtaken by the QRAM process which is a better tool for reflecting seasonal commodity price differences. 46

Energy Probe, Green Energy Coalition (GEC), and Pollution Probe opposed the Company's proposal and, collectively, offered the following arguments: 47

- The removal of seasonality will further exacerbate the competitive disadvantage of natural gas over electricity for water heating. This may have adverse environmental impacts because increased electricity generation would be required with an associated increase in harmful emissions. Gas is generally viewed by these groups as a more "environmentally-friendly" energy source than electricity; 48
- The proposal is inconsistent with the Government of Ontario's electricity policies for time differentiated rates; 49
- Customers abandoning natural gas water heating would reduce the Company's already poor load factor and lead to higher annual costs of providing gas service; 50
- The existing seasonal differential should actually be increased rather than eliminated to more fully capture the peak and off-peak cost behaviour patterns of the utility. 51

The Board has reviewed the evidence and is satisfied that there is only a minimal bill impact associated with removing seasonality. The evidence showed that for Rate 1 customers under different load profiles, the bill impact ranges between an increase of 50 cents per month to a decrease of 7 cents per month. 52

The Board agrees with the Company's view that removing seasonality is financially immaterial to the consumer and that by extension, it should not have any material impact, positive or negative, on consumer behaviour. Given this, the Board has difficulty accepting the proposition that removing seasonality will dissuade conservation efforts, as suggested by the opposing parties. The Board notes that the relative impact of the commodity price substantially overshadows the seasonal differential in distribution rates, which is about 2 cents per m³. The Board agrees with the Company that the commodity price is clearly the more material of the two price signals, so much so as to render the 53

seasonality in the distribution rate immaterial. In terms of conservation efforts, consumers are more likely to be influenced by the commodity price than by the seasonal rate differential in the delivery charge.

With respect to arguments that compare rate seasonality with time differentiation in electricity rates, in the Board's view the two issues are different. The rate seasonality issue relates to a small component of the delivery charge whereas the relatively large electricity commodity charge is highly influenced by time differentiation in terms of intra-day generation demands.

The Board agrees with the Company that the customer is more concerned with the overall bill impact rather than with the impact of the individual elements of the bill. The Board suspects that individual customers are unaware that there is a seasonal differential. If customers are not aware, then it follows that it does not influence their consumption patterns.

The Board also agrees with the Company's argument that the proposed simpler rate structure will lead to less customer confusion and will align its rates with others in the industry.

Based on the evidence, the Board approves the Company's proposal and therefore directs that the Company proceed with its implementation.

Rate 1 Customer Charge

The Company's reasons for the proposed increase from \$10 to \$11.25 per month are as follows:

- It reduces intra-class cross subsidies;
- It is a better reflection of cost causality;
- The proposal is revenue neutral for the utility within the rate class as it represents the shifting of costs from the variable delivery charge to the fixed monthly charge;
- The bill impact is negligible. Larger volume customers will see a slight decrease in their monthly bill and very small-volume customers would see a slight increase. The annual bill increase for a smaller volume Rate 1 sales service customer consuming approximately 1,000 cubic metres of gas per year would be \$9.50. A typical residential customer consuming 3,064 m³ per year would see a decrease of \$0.74 for the year;
- The level of recovery is consistent with the level of cost recovery at Union Gas (Union) for its equivalent residential rate class. At Union, the customer charge will rise from \$10 to \$12 in 2004, and \$14 for 2005;
- Toronto Hydro has a \$14 customer charge.

The Consumers' Association of Canada and the Consumers' Council of Canada (CAC/CCC), GEC, and Pollution Probe and the Vulnerable Energy Consumers Coalition (VECC) opposed the Company's proposal and offered the following reasons for their opposition:

- Concern about the potential adverse customer reaction to the increase;
- The potential negative impact on energy conservation and fuel choice for water heating customers;
- The result would increase bills for small-volume customers who were assumed by intervenors to be low income customers;
- Concern that rate classes other than Rate 1 are not being examined for customer charge increases even though many have a lower percentage of recovery of fixed costs compared to Rate 1.

CAC/CCC put forward a compromise approach that would increase the current charge by only 50 cents to \$10.50.

VECC proposed that if the Board sees a need to increase the charge, then a phase-in period over two to three years would be appropriate to ease the burden on low-income and fixed-income customers.

The Board notes the evidence showing that the customer bill impact is negligible. The greatest customer impact is that some lower volume Rate 1 customers will experience an overall increase in their bill of about \$9.50 per year or 80 cents per month. The Board also notes that these customers constitute only 1 percent of the Company's customer base. The Board further notes that many customers will experience an overall modest decrease in their bill.

There was no evidence to indicate that small volume customers are necessarily also low income customers. This means that there may well be low income customers that actually benefit from the change through a small bill reduction.

The Board notes that from 1996 to 2000, the fixed charge was increased by \$1 each year as it moved from \$7 to \$10. The Board heard no evidence to suggest that these increases were unacceptable to consumers.

From the perspective of pure rate design, the Board accepts the proposition that, all other things being equal, it is desirable to have a higher portion of the fixed costs recovered through the fixed charge. The Board is convinced that the Company's request to increase the fixed cost recovery percentage is desirable at this time.

The Board does not share the views of the parties that suggest that the proposal will result in any change in consumer behaviour and hence, a diminution of conservation efforts. The Board bases this view on the negligible impact this change will have on customer bills.

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The Board notes that the proposed increase would mean that the Company's fixed monthly charge remains below that of Union Gas and Toronto Hydro. This gives the Board a measure of comfort that the proposal is within a range of reasonableness.

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The Board approves this increase in the fixed charge for implementation on October 1, 2004.

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In light of the relatively modest impacts of this proposal, the Board does not believe that a phase-in is warranted.

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In any future review of Board's ROE methodology, consideration should be given to the level of the fixed charge in respect of any assessment of business risk at the utility.

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3 DEMAND SIDE MANAGEMENT (DSM) 82

3.1 BACKGROUND 83

The issue before the Board is Pollution Probe's proposal that the Company develop a commercial, institutional, and industrial large boiler market transformation program as part of its DSM program. These issues are Issues 10.1 and 10.2 on the Issues List. 84

Pollution Probe supported the partial settlement in respect of the 2005 DSM budget and volume target but asked that the Board direct the Company to propose a large boiler market transformation program and associated shareholder incentive program to begin in January 2005. Pollution Probe submitted that its proposal was in the public interest since it would reduce energy bills and assist the Ontario government in its conservation goals through its program to repair and renovate publicly funded schools. 85

3.2 BOARD FINDINGS 86

The Board heard submissions from Pollution Probe, supported by GEC, as follows: 87

- The Company's evidence was to the effect that, absent the Board direction sought by Pollution Probe, implementation of a large boiler market transformation program might be delayed until 2006, resulting in some lost opportunities. Pollution Probe suggested that these lost opportunities would include the Ministry of Education's recently announced \$2.1 billion spending program for infrastructure improvements in publicly funded schools to be undertaken over the 2005-06 school year; 88
- While the Company's DSM programs had greatly lowered customers' bills, the Company's DSM spending, expressed as a percentage of overall revenue requirement, was only half of the North American gas utility average; 89
- Since 1995 only about 10 percent of the Company's industrial customers had participated in the Company's DSM program; 90
- The Company "...has historically invested little in key lost opportunity markets such as new construction and equipment replacement. Moreover, they [the Company] have historically not made long-term market transformation an important goal of their efforts."; 91
- None of the costs of developing and implementing its proposal would be borne by residential customers; 92

- DSM investments are good for the Ontario economy, citing evidence that the ratio of net bill savings to the Company's O&M spending for the fiscal 2004 DSM program was 13.31 to 1.

The Board also received submissions from the Company as follows:

- Development of such a program would require approximately four months;
- Should the Board order the Company to implement such a program during the 2005 Test Year, a mechanism to recover the additional costs was required, preferably an increase in the 2005 DSM budget previously approved in the Settlement Agreement. Failing an increase in the budget, the Company requested that the Board issue an accounting order to establish a deferral account to record the increased costs;
- No costs would be incurred for the market transformation plan until the Board ordered the Company to implement the plan;
- The main issue surrounding Pollution Probe's proposal is one of timing;
- The Board could direct the Company to include a large boiler market transformation program in the strategic plan that the Company will file by January 1, 2005. The Company stated that this was possibly the most practical resolution of this issue given the time required to develop a credible market transformation program.

Other intervenors opposed Pollution Probe citing the following reasons:

- The Company could undertake or develop a large boiler market transformation program within the agreed 2005 budget without unravelling the existing Settlement Agreement. If the program has value for its customers, the Company should have a sufficient incentive to explore the project and offer customers efficient choices in the absence of a formal program;
- Although a large boiler market transformation program could be part of the 2006 DSM plan, Pollution Probe's proposal did not allow the Company sufficient time to research, analyze, and develop such a program.

While the Board believes that a large boiler market transformation program may well provide overall benefits, it found an insufficiency of research and analysis to support that position.

The Board accepts that there have been benefits from DSM spending in the past.

The evidence presented in this case fell short of convincing the Board that implementing a market transformation program, yet to be developed, is of sufficient net value to potentially disrupt the

budget plan settled after stakeholder discussions. The Board therefore will not, on the evidence before it, approve any change to the 2005 DSM budget.

It was suggested in argument that such a program could be implemented in the 2005 test year with no change to the DSM budget by allowing the utility to book the associated costs in a deferral account for later recovery by the utility. In the Board's view, this poses two problems: (i) the program to be implemented has not yet been developed and hence has not undergone review by the Board prior to approval of the accounting order; and (ii) this proposal would increase rate retroactivity at a time when the Board has been endeavouring to reduce rate retroactivity.

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Based on the evidence filed, the Board finds the term "market transformation program", as used by stakeholders, requires clarification. The Board expects future consideration of this issue to include a more precise definition of the term.

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Notwithstanding the preceding, the Board sees merit in the Company's proposal that the Company include a large boiler market transformation program in the strategic plan that the utility will file by January 1, 2005. As usual, consideration of this DSM opportunity should include an objective evaluation of its need and its effectiveness, since neither was proven in this proceeding.

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In view of the Board's finding that the 2005 DSM budget will not be increased, no sharing mechanism related to the proposed market transformation program is required at this time.

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4 OTHER ISSUES 110

The Board has considered some of the other issues that can be dealt with in this Partial Decision. 111
 The Board has decided to dispose of Issue 5.5, the Company's long term commitments for the acquisition of system gas and Issue 11.2, the matter of the request for a Class Action Suit Deferral Account (2005 CASDA).

4.1 ISSUE 5.5 112

The Board notes the following wording in the Settlement Proposal for Issue 5.5. 113

5.5 Matters under review by Enbridge Gas Distribution filed in this proceeding that require commitments to be made prior to the next planned rate application, specifically: 114

- a) entering into long term commitments for the acquisition of system gas; 115
- b) relationships of Enbridge Gas Distribution to projects and/or transactions in which Enbridge Gas Distribution affiliates have an interest; and 116
- c) managing the risk of load erosion related to system gas, as required to support these proposed long term supply commitments. 117

The Company is not in a position to and, as a result, will not bring forward evidence related to this issue for consideration by the Board within the limits of the schedule for the hearing of this case. All parties agree that issue 5.5 continues to have important implications and that it is appropriate for the issue to be addressed as part of the Natural Gas Policy Review. The parties agree that they will be guided by the decision of the Board, released May 27, 2004, on the motion relating to this issue. 118

In light of the fact that there was no evidence put forward on this issue in this proceeding, the Board does not believe that the issue requires any further Board comment, other than that contained in the Board's May 27, 2004 Decision on the Motion. 119

4.2 ISSUE 11.2 - CLASS ACTION SUIT DEFERRAL ACCOUNT (2005 CASDA) 120

The Company has sought Board approval for a 2005 Test Year deferral account, the Class Action Suit Deferral Account (2005 CASDA), relating to its ongoing litigation in respect of its late payment practices. The Company's request was worded as follows: 121

The Company proposes to establish a 2005 CASDA to record costs in defending late payment penalty litigation (the "Garland" case) in the 2005 Test Year, including any judgement against the Company. Any award of costs made to the Company by the Court shall be credited to this account.

In addition, during the course of the proceeding, the Company agreed to include in any CASDA approved by the Board in this proceeding any sums received by the Company from any third party source, which sums mitigate or address in any manner its liabilities arising from the late payment policy litigation.

The Company asked that the 2005 CASDA include:

- The legal costs for both the Company and the plaintiff;
- The costs of actuarial expert advice;
- The costs of analyzing historic billing records; and
- The costs of any judgement against the Company.

It was the inclusion of the cost of any judgement and the inclusion of plaintiff's costs which drew the most argument.

The Company offered the following reasons for inclusion of judgement costs in the deferral account:

- A deferral account for these costs is preferable because of the Company's concern about the impact on earnings resulting from expensing large items if no deferral account is established. If an account is established, the amount recorded may be treated as a regulatory asset or account receivable and thus not expensed in the year;
- It represents the most practical solution until the time that the recovery issue is ripe;
- The Board can deal with it now and need not readdress it until recovery is proposed;
- If the Board denies the account now, the Board will likely be faced with the same arguments it is hearing in this proceeding in a subsequent proceeding.

The Board notes that there was no evidence put forward as to the quantum of the judgement costs or whether, as a certainty, costs would be incurred in the 2005 Test Year, although the Company indicated that some costs are "likely".

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A number of parties argued against the Company's position, mainly on two grounds: first, that the proposal is premature; and second, that the establishment of a deferral account implies an eventual recovery of the amounts from ratepayers.

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Two intervenors, the School Energy Coalition (SEC) and Union Gas (Union), supported the Company's proposal for inclusion of the judgement costs in the account. SEC argued in favour of the account on the ground that the issue is a broad and generic one that affects many companies in many industries. Union said the creation of the account would permit time for the Board to undertake a thorough analysis of the amounts and whether they should be recovered in rates.

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The Board notes the position taken by all parties to the Settlement Proposal, stated as follows:

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Parties acknowledge that the Garland decision of the Supreme Court has implications beyond the Company and will likely require repayment of late payment penalties which are in contravention of the Criminal Code by numerous other gas and electric utilities in Ontario. Whether such payments are properly recoverable in rates is a matter which parties agree is appropriate to be considered by the Board in a funded generic proceeding in which all stakeholders can participate.

140 4.3 BOARD FINDINGS

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Over the years the Board has approved the creation and disposition of the CASDA related to the late payment policy litigation. Typically the deferral accounts encompassed the Company's costs in defending the action and not any amounts related to judgement costs. An exception arose in the atypical 2004 rates proceeding, and was the result of the broad settlement agreement between the Company and the Intervenor in that case.

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The parties were unable to identify any definitive precedent governing or informing the Board's approval of deferral accounts or their constituent elements. It is clear to the Board that one principle that must apply in such determinations is that the Board must have a measure of confidence that the category of costs sought to be included in the deferral account is capable of a fairly definable scope and quantum. While it is in the nature of a deferral account that amounts captured in it may not be definitively assessed or forecast at the time the account is approved, there should be more than a general idea as to the amounts contemplated, and the means by which they will arise.

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The Board is prepared to approve a CASDA for 2005 which includes the Company's legal costs, the costs of actuarial advice and the costs of analyzing historic billing records. However, the Board will not include the costs of any judgement against the Company, nor will it include the plaintiff's costs. The Board does not regard the 2004 CASDA as having any precedential value for the 2005 rates case, and costs recorded in this account have not yet been approved for recovery from ratepayers.

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The Board will not include the judgement costs, including any award of costs against the Company, in the 2005 CASDA for several reasons. First, such inclusion would be premature. One principle

that comes into play is the extent to which the amounts included in the account are likely to arise in the relevant period, which in this case is fiscal year 2005. The Board is not convinced of the Applicant's assertion of the likelihood that such costs will arise in 2005. The timing of the judgement and related orders and their implementation are unknown. The Board also considers that the degree of uncertainty respecting the quantum of damages, if any, and the method of arriving at them makes it inappropriate to include the judgement costs in the 2005 CASDA.

Further, the Board is concerned that by including judgement costs in a deferral account there is a heightened expectation of recovery. The Board wants to be clear though, that excluding these costs from the deferral account at this time does not suggest that the Board will not allow the judgement costs, if any, to be recovered from ratepayers when they arise. The question of ratepayer recovery remains open. The Board expects that there will be developments with respect to the ongoing court proceedings that will lead to a clearer understanding of any amounts and the reasons for them. This greater understanding should assist the Board and the parties in arriving at a determination in respect of a potential ratepayer, or shareholder, responsibility for judgement costs.

Several intervenors argued for a tracking account as opposed to a Board-sanctioned deferral account. The Board sees no reason to order the use of a tracking account. The Board assumes that the Company will have a mechanism for the tracking of any judgement costs for the Board's future consideration

In the Board's view, the Company's concern about earnings impacts is largely related to the timing of any Board decision on ratepayer recovery. The Board is not persuaded to establish a deferral account to ease the Company's concerns about the timing of earnings impacts.

When an appropriate level of detail becomes available regarding the nature and quantum of judgements, the Board will consider a further application by the Company; however, the Board will also consider the parties' request for a Board funded generic proceeding to deal with the matter, as other utilities under the Board's jurisdiction face similar issues.

The Board directs the Company to file a draft accounting order to reflect the Board's findings on this issue.

DATED at Toronto, August 31, 2004

Original Signed by:

Bob Betts
Presiding Member
On Behalf Of The Panel