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PROVINCE OF NEW BRUNSWICK
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March 25, 2010

SENT VIA E-MAIL

To All Parties

IN THE MATTER of an application by Enbridge Gas New Brunswick Limited Partnership to change its Small General Service Residential Electric, Small General Service Residential Oil, Small General Service Commercial, General Service, Contract General Service, Contract Large General Service Light Fuel Oil, Off Peak Service, Contract Large Volume Off Peak Service and Natural Gas Vehicle Fueling distribution rates

And

IN THE MATTER of an application by Enbridge Gas New Brunswick Limited Partnership to change its Contract Large General Service Heavy Fuel Oil distribution rates.

Flakeboard Company Limited ("FCL"), by letter dated March 19, 2010, informed the New Brunswick Energy and Utilities Board ("Board") that it intended to bring a motion before the Board to strike out the report prepared by Mr. Robert D. Knecht dated March 12, 2010. This report was filed by the Public Intervenor in the matter of the Board's review of an application by Enbridge Gas New Brunswick Limited Partnership ("EGNB") to change distribution rates for all of its customer classes, except the HFO class (Board proceeding number 2009 017). The same report was filed by the Public Intervenor with respect to the Board's review of an application by EGNB to change the distribution rates for the HFO class (Board proceeding number 2010 001)

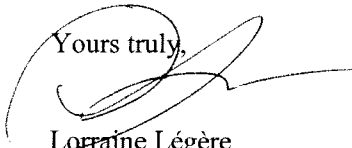
The Board, on March 22, 2010, informed the interested parties that it would hear the motion of FCL on March 23, 2010. At that time, the Board heard argument from FCL, the Public Intervenor, EGNB and Atlantic Wallboard LP.

The Board has considered all of the arguments and has carefully reviewed the report prepared by Mr. Knecht dated March 12, 2010, and makes the following comments.

Evidence is only admissible if it is relevant and will be of assistance to the Board in making its decision. The Board in two decisions, one dated January 22, 2010 and the other dated February 16, 2010, provided guidance as to the nature of evidence that would be acceptable in the current proceedings.

The Board finds that a significant portion of the report is not relevant for the proceedings for which it has been filed and is not in compliance with the two decisions identified above. However, the Board finds that parts of the report are admissible. Attached is a redacted report which will be accepted by the Board as evidence in each proceeding.

Yours truly,



Lorraine Légère
Secretary of the Board

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IEC

BEFORE THE NEW BRUNSWICK
ENERGY AND UTILITIES BOARD

IN THE MATTER OF:
ENBRIDGE GAS NEW BRUNSWICK

Application to Change Distribution
Rates

DOCKET No.: NBEUB 2009-017

12 March 2010

prepared on behalf of:
New Brunswick Public Intervenor

prepared evidence of:
Robert D. Knecht
Industrial Economics, Incorporated
2067 Massachusetts Avenue
Cambridge, MA 02140

REDACTED

1. INTRODUCTION

1 PLEASE STATE YOUR NAME AND BRIEFLY DESCRIBE YOUR BACKGROUND.

2 My name is Robert D. Knecht. I am a Principal and the Treasurer of Industrial
3 Economics, Incorporated ("IEc"), a consulting firm located at 2067 Massachusetts
4 Avenue, Cambridge, MA 02140. As part of my consulting practice, I prepare analyses
5 and expert testimony in the field of regulatory economics. In Canada, I have submitted
6 expert evidence in regulatory proceedings in Québec, Ontario, Alberta, New Brunswick,
7 Nova Scotia, Manitoba, and Prince Edward Island. In regulatory proceedings in New
8 Brunswick, I submitted evidence before the New Brunswick Energy and Utilities Board
9 ("the Board") and its predecessors in matters regarding New Brunswick Power in
10 1991/92, 2005/06, and 2007, and in matters regarding Enbridge Gas New Brunswick,
11 L.P. ("EGNB") in 2009. I have also presented expert evidence in matters relating to the
12 rate regulation of natural gas distribution companies ("NGDCs") in Ontario, Alberta and
13 Pennsylvania.

14 I obtained a B.S. degree in Economics from the Massachusetts Institute of Technology in
15 1978, and a M.S. degree in Management from the Sloan School of Management at M.I.T.
16 in 1982, with concentrations in applied economics and finance. My *curriculum vitae* and
17 a schedule of my expert evidence presented to regulatory tribunals during the past five
18 years are attached as Exhibit IEC-1.

19 WHAT ARE THE KEY FEATURES OF THE CURRENT RATE REGULATION THAT IS
20 APPLIED TO EGNB?

21 The current regulatory régime recognizes that EGNB is in a Development Period. As
22 established by the Board in its Decision at Docket No. NBEUB-2009-006, the primary
23 determinant for Development Period status is that EGNB's total costs exceed the
24 revenues that EGNB can earn under Board-approved rates. Total costs include both all
25 going-forward costs of providing service, plus past-service costs associated with
26 regulatory deferrals and deferred O&M costs that the Board has determined to be prudent
27 but which EGNB has been unable to recover in rates. Because EGNB's total costs
28 currently exceed revenues, a shortfall exists which is deferred for potential future
29 recovery. In addition, at present, the Development Period return on equity approved by
30 the Board is considerably higher than equity returns awarded to mature Canadian
31 NGDCs.

32 In general, EGNB's rates are established based on market conditions, such that the
33 delivered price of natural gas is set at a competitive discount to the delivered cost of
34 competing fuels. Rate classes are generally defined based on the size of the customer, but
35 the small general service class is differentiated between customers who have converted to
36 gas from oil heat and customers who have converted from electric heat. The competitive
37 discount relative to the delivered price of competing fuels is that which is deemed
38 necessary to encourage customers to convert to natural gas, and to offset the costs and
39 disruptions associated with the conversion. The competitive discounts generally range
40 from 5 to 20 percent of the cost of the competing fuel.

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1 Distribution rates are calculated by taking the delivered cost of the relevant competing
2 fuel for a typical customer in each class, deducting the competitive discount, and
3 subtracting the commodity price of gas, leaving the revenues available for distribution
4 service. Rates for each class are then defined based on the charges necessary to produce
5 those revenues for the typical customer. For the smaller classes, EGNB uses a customer
6 charge and commodity charge design; for the larger customer classes, a demand charge
7 and commodity charge structure is used.

8 At least heretofore, allocated costs have not been a factor in setting EGNB's rates.

9 WHAT IS THE PURPOSE OF YOUR EVIDENCE IN THIS PROCEEDING?

10 In its decision at Docket No. NBEUB-2009-006, the Board directed that EGNB file a cost
11 allocation or cost-of-service study ("COSS"). Consistent with that order, on 15 January
12 2010, EGNB filed a COSS, with supporting evidence from EGNB witnesses Messrs.
13 Charleson and LeBlanc, and from consulting expert Mr. H. Edwin Overcast of Black &
14 Veatch Corporation ("B&V"). The filed materials included three general proposals
15 related to cost allocation and rate design, namely:

- 16 • Development of a proposal for modified rate classes, to which costs are
17 allocated in the COSS, based generally on customer load characteristics
18 rather than on competing fuels;
- 19 • Allocation of the full 2010 revenue requirement to all rate classes;
- 20 • A proposal for the tariff *structure* for each rate class, albeit without any
21 specific proposals for tariff charges.

22 The relevance of these analyses for the instant proceeding was put to the Board. In its
23 Motions Day ruling, the Board opined:

24 *Developing a new rate making methodology for gas distribution in New Brunswick*
25 *will be an important step for the Board, EGNBLP and its customers. It will be critical*
26 *to have the best available evidence. To develop a new rate making methodology prior*
27 *to completing the review of the cost of service study and the Return on Investment*
28 *would not provide the Board with the best evidence. To develop a new methodology*
29 *during a rate application would also provide less opportunity for EGNBLP and other*
30 *parties to develop and review evidence and proposals.*

31 *The Board will not approve, during the review of these two rate applications, a rate*
32 *making methodology to replace the existing system going forward.*

33 *The Board wishes to make it clear that parties may submit any evidence which is*
34 *relevant to the applications being heard at this hearing. While the present rate setting*
35 *methodology begins with the Board approved formula, the Board has an obligation to*
36 *inquire into whether the rates produced by the formula are just and reasonable, and if*
37 *they are not, to fix rates which are just and reasonable. Any evidence which would*
38 *assist the Board in determining whether the proposed rates are just and reasonable is*
39 *relevant. Any evidence suggesting "such other rates" as the Board may find*
40 *reasonable in this instance is also relevant, but evidence whose purpose was to*

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1 suggest a rate making methodology for use in future applications would not be
2 relevant.

3 With respect to the Cost of service study, and the interrogatories permitted in relation
4 to it, the issue is one of relevance. Questions which relate to a matter in issue in this
5 application are relevant. Whether the rates proposed in the application are just and
6 reasonable is a matter in issue in this application, as is what "other rates" the Board
7 might find reasonable. The accuracy of the cost of service study and the correctness of
8 the proposals contained therein are not matters in issue in this application.

9 As I understand it, the Board determined (quite correctly, in my view) that a new
10 ratemaking methodology for EGNB would require, at a minimum, a thorough review of
11 the COSS, as well as an evaluation of the appropriate return on equity for EGNB. The
12 Board also stated that EGNB's filed COSS could not be contested for accuracy in these
13 proceedings.

14 However, for the purposes of this proceeding, the Board indicated that it would consider
15 all evidence which would assist it in determining whether the market-based formula
16 produces just and reasonable rates. Because most regulators do consider COSS results in
17 developing just and reasonable rates, the New Brunswick Public Intervenor asked me to
18 evaluate whether the results of the uncontested COSS filed by EGNB should be
19 considered by the Board as relevant evidence in this proceeding.

2. RELEVANCE OF FILED COST OF SERVICE STUDY

20 **IS THE COSS FILED BY EGNB RELEVANT FOR SETTING RATES IN THIS PROCEEDING?**
21 I conclude that it is not. As such, I agree with EGNB's response to Flakeboard IR No. 8,
22 which indicates that "... EGNB notes that the allocations are based on assumptions that
23 have not been tested in a hearing and can change significantly based on changes to some
24 of these assumptions."

25 More specifically, I have four reasons supporting my conclusion.

26 • First, in the filed COSS, EGNB does not use the current customer rate
27 classes. Instead, EGNB proposes to establish new rate classes based more
28 on the size of a customer's load than on the competing fuel. Because this
29 proposal has not been evaluated or contested, the allocation of costs to
30 these classes has little or no relevance to the current proceeding.

36 • Third, EGNB's filed COSS contains a host of assumptions and parameters
37 that have not been evaluated and contested. Alternative methods,
38 corrections and analyses could result in significant cost shifts from those
39 presented in the filed study.

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36 CAN YOU PROVIDE AN ILLUSTRATION OF THE SENSITIVITY OF EGNB'S FILED COSS
37 TO ALTERNATIVE ASSUMPTIONS?

38 I can, but I offer the very strong caveat that this is an illustration and not a
39 recommendation. For the purposes of this illustration, I modified EGNB's filed COSS as
40 follows:

- 1 • Deferred costs, including both the regulatory deferral and the development
2 O&M, were allocated on an energy basis. That is, each rate class is
3 assigned the same per-GJ cost.
- 4 • Mains costs were classified as 42 percent customer-related and 58 percent
5 demand-related, based on a rough zero-intercept analysis. Mains demand-
6 related costs were allocated using EGNB's unadjusted peak demand
7 allocator.

8 The impact of these two changes is shown in Table IEc-1 below.

	EGNB Filed	Illustration	% Difference
Small General	\$56.54	\$33.06	- 41.5%
Mid General	\$13.79	\$13.77	- 0.1%
Large General	\$ 8.50	\$12.15	+ 42.9%
Contract General	\$ 4.62	\$9.54	+106.5%
Ind. Contract General	\$ 2.46	\$ 7.73	+214.2%
Off-Peak Service	\$22.83	\$17.71	- 22.4%
Total	\$13.43	\$13.43	0.0%

CONCLUSIONS AND 21
RECOMMENDATIONS

My conclusions and recommendations to the Board are as follows:

- 24 • EGNB's filed COSS should not be used for actual rate design without
25 being fully evaluated and contested;