DECISION

IN THE MATTER of an application by Enbridge Gas New Brunswick Inc., to change its Contract Large General Service LFO distribution rate

April 9, 2008

NEW BRUNSWICK ENERGY AND UTILITIES BOARD

IN THE MATTER OF an application by Enbridge Gas New Brunswick Inc. for approval of a change to its Contract Large General Service LFO distribution rate.

NEW BRUNSWICK ENERGY AND UTILITIES BOARD ("BOARD"):

CHAIRMAN:	Raymond Gorman, Q.C.
VICE-CHAIRMAN:	Cyril Johnston
MEMBERS:	Edward McLean Robert Radford Steve Toner
COUNSEL:	Ellen Desmond

APPLICANT:

Enbridge Gas New Brunswick ("EGNB")	Len Hoyt, Q.C.

FORMAL INTERVENORS:

Atlantic Wallboard LP/J.D. Irving Limited ("AWL")	Christopher Stewart
Canadian Manufacturers & Exporters NB Division ("CME")	David Plante
Flakeboard Company Limited ("FCL")	Gerald Lawson

Informal Intervenors:

Canadian Restaurant and Food Services Association

Competitive Energy Services

Department of Energy

Ganong Brothers Limited

Public Intervenor

Sucor Limited

On November 5, 2007, Enbridge Gas New Brunswick Inc. ("EGNB") applied to the New Brunswick Energy and Utilities Board (the "Board"), pursuant to Sections 52 and 56 of the *Gas Distribution Act, 1999* (the "Act"), for an order or orders approving changes to its Contract Large General Service LFO ("LFO") distribution rate.

EGNB is the general franchisee under a general franchise agreement dated August 31, 1999 ("GFA") with the province of New Brunswick. The GFA (which was filed with the Board as part of EGNB's 2000 rate application) authorizes EGNB to distribute natural gas and provide customer services in the Province of New Brunswick.

The 2000 rate application resulted in a decision, from the New Brunswick Board of Commissioners of Public Utilities dated June 23, 2000, wherein the Board approved EGNB's market-based approach for setting its distribution rates during the development period. The objective of EGNB's market-based approach was to provide potential end use customers with the economic incentive to convert to, and continue to use, natural gas and to make use of the distribution system that EGNB committed to build in New Brunswick.

By Order of the Board dated November 7, 2007, EGNB was required to publish a Notice of the application in various New Brunswick newspapers and was further required to provide a copy of the notice to each of EGNB's then current LFO customers and to each certified gas marketer. The Notice advised the public of a pre-hearing conference scheduled for the Board's offices on Friday, December 7, 2007 and set out the procedure for parties to follow if they wished to intervene in the proceedings

Three parties indicated that they wished to become formal intervenors, namely Atlantic Wallboard Limited Partnership/JD Irving Limited ("AWL"), Canadian Manufacturers and Exporters NB Division ("CME") and Flakeboard Company Limited ("FCL"). CME did not take any further part in the hearing process. In addition a number of parties indicated their desire to become informal intervenors, namely Canadian Restaurant and

Food Services Association, Competitive Energy Services, Department of Energy, Ganong Brothers Limited, Public Intervenor and Sucor Limited

On January 15, 2008 AWL submitted a Motion to the Board that requested the following remedy:

> *"The within matter be adjourned and the Board conduct a hearing into the appropriate rate making methodology to be utilized to establish distribution rates for EGNB's contract Large General Service – Light Fuel Oil class."*

AWL's motion was heard by the Board on January 17, 2008. All parties agreed that, at some point in time, it would be appropriate to move from the currently approved market-based method of setting rates to some other method. This alternate method would most likely be a form of cost-based rate setting.

The issue that arose during the Motion involved the timing of when such a change should occur. EGNB maintained that it was still in the "development period" and therefore it would not be appropriate to make a change to the rate-setting methodology at this time. AWL and FCL argued that, at least for the LFO class, the "development period" was over and the market was mature. Much of their argument was based on the fact that there are 20 customers in this class and EGNB is only able to identify five other potential customers in the Province of New Brunswick at this time. Accordingly the intervenors claimed that in order for the Board to set rates for the LFO class, that are both just and reasonable, they must be based on a cost setting method, or at the very least, a method that recognizes the costs associated with this class of customers.

To understand this issue fully, a little background is useful. When the delivery of natural gas in New Brunswick by EGNB began in 2000, it was recognized that, given the significant capital investment required to begin operations and the limited number of customers that would initially be on the system, it would be impossible to charge rates based on the full cost of operation. This fact was recognized by both the Province of New Brunswick and EGNB, as signatories to the general franchise agreement, as an essential element and was accepted by the Board in its first rate setting decision for EGNB.

In its June 2000 decision, the Board stated that the use of a non-traditional regulatory framework would be appropriate during the period of time required to move from a "greenfield" situation to a more established natural gas industry. This period is referred to as the "development period". Use of a non-traditional regulatory framework is permitted by Section 67(2) of the *Energy and Utilities Board* Act which states:

> *"67(2) in approving or fixing just and reasonable tolls and tariffs, the Board may adopt any other method or technique that it considers appropriate, including an alternative form of regulation".*

Up to the present time EGNB's rates have been set using a market-based methodology. This method establishes rates that provide an incentive to convert to, and to continue to use, natural gas. As indicated earlier, these rates are not based on costs. EGNB has, based on the premise that a market-based method would be used to set rates during the "development period", invested a significant amount to establish its gas distribution system in New Brunswick. The capital costs associated with this investment have been approved by the Board as legitimate expenses for regulatory purposes. Together with the operating costs, they make up the total costs for EGNB. The revenues received by EGNB, from rates set using a market-based method, have not been sufficient to cover EGNB's total costs. The difference between the actual costs of providing service and the revenues received from the market-based rates are recorded in a deferral account. The Board has found that the use of such a method provides rates that are just and reasonable.

In its decision on the AWL Motion dated January 18, 2008, the Board stated as follows:

"The Board, based on the evidence, is convinced that the "development period" has not yet ended nor will it in the near future. The Board will, therefore, proceed to set rates in this application using the market-based method".

The Deferral Account as approved by the Board had a balance of $102.2 million as at December 31, 2006. It is essential, for the long term future of the natural gas system in New Brunswick, that the deferral account not continue to grow. During the "development period" it is important that whenever circumstances permit, prices should be set so as to address this and other issues. EGNB has demonstrated that, if market conditions change, it will apply to lower its rates and the Board expects that EGNB will continue to do so. The Board finds that the use of a market-based method to set rates is appropriate during the "development period" and that it will provide the proper balance between the interests of EGNB's customers and EGNB's shareholders.

The market-based method sets delivery rates by calculating the cost of an alternative energy source, deducting the cost of the natural gas commodity and then setting delivery rates at an amount which provides the customer with savings in comparison to the energy alternative. The estimated amount of the savings is pre-determined and referred to as the "target savings level". In order for the market-based method to produce rates which are just and reasonable, and which balance the interests of EGNB's owners and EGNB's ratepayers, it is imperative that the calculations relating to the cost of alternative energy be accurate and that the target savings levels be appropriate.

The formula used by EGNB to derive its proposed distribution rates for the LFO class is complex. It contains a number of elements that require the application of judgment. Changes to the values of the elements can have substantial impacts on the eventual distribution rates. The Board does not intend to canvas fully in this decision every issue related to the determination of each element, but feels it is appropriate to review in some detail the manner in which the rates are derived and to discuss some of the issues which arose at the hearing.

The first element is the calculation of the forecast retail oil price; light fuel oil being the energy alternative for this rate class. EGNB begins the calculation by taking an average of a 21-day sample of crude oil prices over the forecast period and then applying a series of calculations to convert crude oil prices into a forecast retail oil price for New Brunswick in Canadian dollars. The chief area of concern for the intervenors was the length of that sample period. The intervenors took the position that 21 days was too short a period of time to use as the basis for a maximum distribution rate that would be in effect for at least one year. John Reed, an expert testifying on behalf of AWL, presented calculations using sample periods of 60, 90 and 365 days.

The second element used to derive rates is the target savings level. For the LFO class 10% has been the figure most recently used. Mr. Reed proposes a 15% target savings level. EGNB asserts that the current target of 10% is appropriate as, in its view, the amount is sufficient to attract and retain customers.

The third element used to calculate the distribution rate is the price of the natural gas commodity itself. Since the market based system is premised upon a comparison of the total cost of using natural gas with the cost of an alternate source of energy, accurate forecasting of the commodity price is important. The length of the sample period is an issue with respect to the price of natural gas, but the issue is made more difficult by the lack of transparency in the natural gas market. Put simply, neither EGNB nor the Board can state with certainty what price the various members of this class pay for natural gas. EGNB had previously used its Enbridge Utility Gas ("EUG") price for this element and proposes changing to its Enbridge Variable Product ("EVP") price.

Two further elements that are subject to some debate are the typical annual gas consumption and the average monthly contract demand. EGNB has used estimates for both these items, using a figure of 31,745 GJ for annual oil consumption and 350 GJ for monthly demand. In response to interrogatories from Board staff, the forecast usage for 2008 of 31,205 GJ and 357 GJ for average contract demand was obtained. EGNB used the estimates from their previous application since their updated estimates were similar.

As an example of the element of judgment which goes in to the derivation of rates, it is noteworthy that EGNB does not include the two largest customers in the LFO class when calculating oil consumption or contract demand.

The Board has stated previously, and repeated in this decision, that the development period is not yet over and will not end in the near future. In the near term the Board will continue to apply the market-based method to set rates for the distribution of natural gas. The Board continues to believe that this method can balance the interests of the utility and its customers. The Board believes, however, that in order to ensure that the market based system continues to produce rates that are just and reasonable, all of the elements used in deriving the rates must be subjected to close scrutiny. The Board will therefore convene a technical conference, to be followed by a generic hearing. The purpose of this process will be to examine all elements of the derivation formula to ensure that the target savings levels are appropriate and that they are achieved through the use of the formula. This process will cover all rate categories and will be more fully described in the Board's upcoming decision relating to the other rate categories. This process is separate and apart from the process directed by our Decision of January 18th, 2008, which will focus on the manner of determining the end of the development period and related issues.

The Board wishes to make it clear that all elements of the formula will be open for debate at the technical conference and hearing and that the Board will not be bound by previous decisions relating to elements of the formula, including this one.

The Board shall set the rates for the present application based on the evidence provided in this proceeding.

One significant issue before the Board is the appropriate length of the sample period. The Board is satisfied that a one-month period, using 21 days of data is too short a period of time upon which to base a maximum rate that will be in force for at least a year. Similarly, the Board concludes that a 365-day period is too long to provide an accurate view in a time of rapidly changing energy prices. For the purposes of this application, the

Board finds that the use of the 60-day calculations found in Mr. Reed's evidence is appropriate.

The Board continues to believe that the 21-day sample period is reasonable with respect to the use of rate riders by EGNB, as a shorter period will enable EGNB to react quickly to changing markets.

The Board is not persuaded that the target savings level should be increased from 10% to 15%. Based on the evidence at the Hearing the Board finds that a rate of 10% is sufficient for EGNB to attract and retain customers in this class.

With respect to the calculation of typical annual oil consumption and average monthly demand, the Board will accept the method used by EGNB, that is to say the exclusion of the two largest customers on the basis that their inclusion would skew the results. The Board will use the most recent estimate, rather than the estimates carried over from the last application.

For the purposes of its calculation the Board will use the table filed in Mr. Reed's report setting out his calculations with a 60-day average of oil and gas prices representing approximately two months. These figures were entered in to the evidence and were not challenged by any party. They are broadly consistent with the evidence of the applicant.

Attached to this decision, as Table 1, is a calculation of the LFO distribution rate prepared using Mr. Reed's figures, modified to retain a target savings level of 10% and to use the most recent estimates for forecast annual oil consumption and average monthly contract demand. The result is a distribution rate of $4.0861/GJ.

The Board approves the following rates for the Contract General Service- LFO Class immediately upon EGNB filing with the Board new rate schedules that indicate the approved rates pursuant to Section 56 of the Act:

Demand Charge for GJ of Contract Demand ($/GJ)	5.20
For the first 33,000 GJ delivered per month ($/GJ)	4.0861
For the next 25,000 GJ delivered per month ($/GJ)	0.1900
For volumes delivered in excess of 58,000 GJ per month ($/GJ)	0.0800.

Dated at the City of Saint John, New Brunswick this 9th day of April 2008.

Raymond Gorman, Q.C., Chairman

Cyril W. Johnston, Vice-Chairman

Edward McLean, Member

Robert Radford, Member

Steve Toner, Member

Table 1

Calculation of Distribution Rate

1	Retail Oil Price ($/l)	0.6126
2	Retail Oil Price ($/GJ)	15.84
3	Typical Oil Consumption (l)	807,248
4	Typical Oil Consumption (GJ)	31,205
5	Annual Oil Cost ($)	494,520
6	Target Savings Level (%)	10
7	Target Annual Savings ($)	49,452
8	Annual Natural Gas Cost ($)	445,068
9	Annual Natural Gas consumption ($)	31,205
10	Burner Tip Price ($)	14.26
11	Commodity price ($/GJ)	9.46
12	Distribution Rate ($/GJ)	4.8000
13	Total Distribution Charge ($)	149,784
14	Monthly Demand Charge ($/GJ)	5.20
15	Average Monthly Contract Demand (GJ)	357
16	Annual Demand Charge ($)	22,276.80
17	Annual Delivery Charge ($)	127,507
18	Delivery Charge ($/GJ)	4.0861