



National Energy Board

Reasons for Decision

**TransCanada PipeLines
Limited**

RH-1-97

September 1997

**1997 Tolls &
FST Conversion Proposal**

National Energy Board

Reasons for Decision

In the Matter of

TransCanada PipeLines Limited

Application dated 19 March 1997, as amended
29 April 1997, for new tolls effective
1 January 1997;

and

Application dated 6 May 1997 for approval of
TransCanada's FST Conversion Proposal.

RH-1-97

September 1997

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Abbreviations

Act	<i>National Energy Board Act</i>
ADOE	Alberta Department of Energy
AEC	Alberta Energy Company Ltd.
AFUDC	Allowance for Funds Used During Construction
ANR	ANR Pipeline Company
AO	Amending Order
Board	National Energy Board
CAPP	Canadian Association of Petroleum Producers
Centra	Centra Gas Ontario Inc.
CDA	Central Delivery Area
Company	TransCanada PipeLines Limited
Consumers	Consumers' Gas Company Ltd., The
DDA	Distributor Delivery Area
EDA	Eastern Delivery Area
FERC	Federal Energy Regulatory Commission
FST	Firm Service Tendered
FT	Firm Transportation
Gaz Métropolitain	Société en commandite Gaz Métropolitain
GJ	gigajoule
GPUC	Gas Plant Under Construction
Great Lakes	Great Lakes Gas Transmission Limited Partnership
GST	Goods and Services Tax
Incentive Settlement	TransCanada's Incentive Cost Recovery and Revenue Sharing Settlement
IT	Interruptible Transportation

NOVA	NOVA Gas Transmission Limited
NEB	National Energy Board
OM&A	Operations, Maintenance & Administrative Expense
RFP	Request for Proposal
RH	Rate Hearing, number and year (e.g. RH-4-93)
ROFR	Right of First Refusal
SCC	Stress Corrosion Cracking
STFT	Short Term Firm Transportation Service
STS	Storage Transportation Service
TBO	Transmission By Others
TTF	Tolls Task Force
TransCanada	TransCanada PipeLines Limited
Union	Union Gas Limited

Glossary of Terms

(Explanations for certain terms used in these Reasons which appear infrequently in Board reports or which may be applicable to TransCanada only are provided for the reader's convenience.)

C1	Firm Service offered by Union Gas Limited from Parkway to Dawn.
FST Agreement	The FST Settlement Agreement was a negotiated agreement between CAPP, Consumers, Union and TransCanada concerning a revised suite of services approach for calculating the FST differential and the allocation of it between upstream and downstream for the 1996 Test Year.
GH-2-97	Hearing Order in Respect of TransCanada's 1998 Facilities Application.
Incentive Cost Recovery and Revenue Sharing Settlement	Settlement reached by parties with respect to the components of TransCanada's Revenue Requirement, (except for those cost of capital related matters determined in RH-2-94), effective for the years 1996 - 1999.
M12	Firm Service offered by Union Gas Limited from Dawn to Parkway.
Part IV	The Part of the NEB Act which deals with Traffic, Tolls and Tariffs.
RH-2-94	Hearing Order in respect of Multi-Pipeline Cost of Capital.
RH-3-94	Hearing Order in respect of TransCanada's application for new tolls effective 1 January 1995.
RH-2-95	Hearing Order in respect of TransCanada's application for new tolls effective 1 January 1996.
TGI-7-96	Order which established interim tolls for TransCanada effective 1 January 1997. Amending orders AO-1-TGI-7-96 and AO-2-TGI-7-96 established revised interim tolls effective 1 April 1997 and 1 May 1997 respectively.
Tolls Task Force	A joint industry Task Force initiated by TransCanada. Its membership is comprised of a wide cross-section of the natural gas industry, including representatives of the producing, marketing, brokering, pipeline, provincial government, local distribution and industrial end-user sectors.

Recital and Appearances

IN THE MATTER OF the *National Energy Board Act* ("the Act") and the Regulations made thereunder; and

IN THE MATTER OF an application dated 19 March 1997 by TransCanada PipeLines Limited and revised on 29 April 1997 pursuant to Part IV of the Act for Orders fixing tolls for the 1997 Test Year; and

IN THE MATTER OF an application dated 6 May 1997 by TransCanada with respect to the conversion of FST; and

IN THE MATTER OF the National Energy Board Hearing Order RH-1-97.

HEARD in Calgary, Alberta on 28, 29 and 30 July 1997.

BEFORE:

J.A. Snider	Presiding Member
R. Priddle	Member
R.D. Revel	Member

APPEARANCES:

J.M. Murray J. Watson	TransCanada PipeLines Limited
N.J. Schultz	Canadian Association of Petroleum Producers
T.G. Kane	ANR Pipeline Company
J.H. Farrell	Consumers' Gas Company Ltd., The
A.S. Hollingworth	Portland Natural Gas Transmission System
M. Voinorosky	ProGas Limited
G.K. Cameron	Union Gas Limited and Centra Gas Ontario Inc.
R. Estabrooks C.J.C. Page	Alberta Department of Energy
L.A. Boychuk	Board Counsel

Overview

(Note: This overview is provided solely for the convenience of the reader and does not constitute part of the Decision or Reasons, to which the reader is referred for detailed information.)

The Application

On 19 March 1997, TransCanada applied to the Board for new tolls effective 1 January 1997. On 29 April 1997, TransCanada filed revisions to its Application. On 6 May 1997, TransCanada applied to the Board for approval to enter into a combination of storage, balancing and transportation contracts, and to purchase "start-up" gas to replace the FST which Consumers and Union have elected to convert to FT service.

The Hearing

The hearing was held in Calgary on 28, 29 and 30 July 1997.

Revenue Requirement

The Board has approved TransCanada's applied-for Net Revenue Requirement for toll design and cost allocation purposes of \$1,704.3 million for the 1997 Test Year subject to any changes that may result from decisions taken by the Board in these Reasons.

Rate Base

The Board has approved TransCanada's applied-for rate base of \$7,427.1 million for the 1997 Test Year.

Rate of Return

The Board has approved a rate of return on rate base of 9.85% for TransCanada in 1997. This includes a rate of return on common equity of 10.67% which was approved by the Board on 14 March 1997 in accordance with the Board's RH-2-94 decision.

Allocation Units Used in TransCanada's Toll Design Methodology

The Board approved the continuation by TransCanada of its existing methodology of using metered volumes for calculating its load centres for the purposes of calculating tolls. In this regard, the Board also approved TransCanada's proposed changes to the methodology for determining the volumes to be used at Parkway and Dawn in the calculation of load centres. The Board also directed TransCanada to adjust the volumes at Sabrevois, Dawn-Export, and Spruce, to reflect the removal of export volumes which have incorrectly been included in the load centre calculations.

FST Conversion

The Board approved TransCanada's proposal to replace FST with FT service by entering into a combination of storage, balancing and transportation arrangements, and by purchasing start-up gas. The Board also approved the specific contractual arrangements that TransCanada has entered into with AEC, ANR, Great Lakes, and NOVA, as well as its proposed arrangements with Union.

Chapter 1

Background and Application

By application dated 19 March 1997 and revised on 29 April 1997, TransCanada applied to the NEB pursuant to sections 59, 60 and 65 of the Act for orders fixing final tolls that the Applicant may charge in respect of transportation services rendered by the Applicant effective 1 January 1997, and disallowing any existing tolls or portions thereof that are inconsistent with the tolls so fixed.

In its letter dated 26 March 1997, the Board acknowledged receipt of TransCanada's 1997 Tolls Application and gave parties the opportunity to submit to the Board, by 15 April 1997, any comments that they may have had regarding TransCanada's application. This comment period was in accordance with the terms of TransCanada's Incentive Settlement.

On 15 April 1997, Consumers submitted a complaint to the Board regarding the allocation units used by TransCanada to calculate tolls, but indicated that it wished to negotiate with TransCanada to attempt to resolve this matter and undertook to advise the Board of the outcome by 30 April 1997.

On 30 April 1997, the Board approved TransCanada's request for revised interim tolls effective 1 May 1997 (Order AO-2-TGI-7-96). The request for interim tolls was based on revisions to TransCanada's 1997 Tolls Application.

In letters dated 30 April 1997 and revised 1 May 1997, Consumers indicated that it had been unable to resolve the allocation units issue with TransCanada and requested that the Board establish a written proceeding to deal with the matter.

By letter dated 6 May 1997, TransCanada applied, pursuant to sections 59 and 70 of the Act, for approval to enter into a combination of storage, balancing and transportation contracts, and to purchase "start-up" gas to replace the FST which Consumers and Union have elected to convert to FT service.

On 8 May 1997, the NEB indicated that it would consider Consumers' complaint regarding TransCanada's allocation units and any other issues related to the revisions contained in TransCanada's revised application dated 29 April 1997 by way of an oral hearing and that a Hearing Order would be issued shortly.

On 22 May 1997, the Board issued Hearing Order RH-1-97 and added TransCanada's FST Conversion proposal to the List of Issues. On 23 May 1997, the Board indicated that the hearing would take place in Calgary starting on 28 July 1997.

On 4 June 1997, TransCanada advised the Board that it would be filing proposed tariff changes in RH-1-97 that would affect the contract renewal rights of all FT, FST and STS shippers.

On 10 June 1997, the Board advised parties that contract renewal rights would be added to the RH-1-97 List of Issues.

The Board then received a letter from CAPP dated 9 June 1997, submitting that the issue of contract renewal rights is significant and controversial and transcends the scope of the issues that led to the

RH-1-97 proceeding. CAPP submitted that the existing timetable would not provide parties with sufficient time to address this issue and urged the Board to establish a separate proceeding and to provide parties with more time to adequately deal with the contract renewal rights issue.

On 12 June 1997, TransCanada filed its explanatory and written direct evidence on the allocation units issue as well as its Right of First Refusal ("ROFR") proposal concerning contract renewal rights.

After considering the views of parties, the Board advised on 13 June 1997, that it would hear the contract renewal rights issue separately in a second phase (Phase 2) of the RH-1-97 public hearing commencing 19 August 1997.

On 19 June 1997, CAPP proposed that TransCanada's expansion policy requirements concerning the market and supply evidence to be provided by expansion shippers also be included in Phase 2 of the Board's RH-1-97 proceeding as this issue is related to contract renewal rights.

In a letter dated 3 July 1997, the Board asked parties to comment on CAPP's proposal of 19 June 1997.

In its comments dated 11 July 1997, TransCanada requested that the Board allow the Company to amend its Application by replacing its ROFR proposal with a proposal calling for a 12-month notice period and a two-year minimum contract term. TransCanada also requested that the time fixed by the Board for the commencement of Phase 2 of RH-1-97, be extended from 19 August 1997 to 22 September 1997, including the adoption of TransCanada's proposed timetable.

After considering parties' comments, the Board, on 18 July 1997, advised that Phase 2 of RH-1-97 would be severed from RH-1-97 and a separate proceeding established to address TransCanada's contract renewal rights issue and its expansion policy requirements. On 23 July 1997, the Board published Hearing Order RH-3-97 in this regard.

The RH-1-97 public proceeding, which lasted three days, was held in the Board's Hearing Room in Calgary, Alberta on 28, 29 and 30 July 1997. The following matters were considered:

- a) The allocation units issue;
- b) Revisions to TransCanada's 1997 Tolls Application filed 29 April 1997; and
- c) The FST conversion issue.

Chapter 2

TransCanada's Incentive Cost Recovery & Revenue Sharing Settlement

The Board, in its RH-2-95 Phase 2 Decision, approved an Incentive Settlement that was negotiated between TransCanada and its stakeholders, as represented by the TTF. The Incentive Settlement is to be applied in determining TransCanada's Net Revenue Requirement utilized in the calculation of the Company's tolls.

As indicated above, the parties in negotiating the terms of the Incentive Settlement, agreed that certain elements of TransCanada's Cost of Service would continue to require the Board's approval. These Reasons for Decision reflect these requirements and, as well, provides an overview of the other elements of TransCanada's total Cost of Service. Appendix II provides a summary of some of the key provisions of TransCanada's Incentive Settlement¹.

¹ The full text of TransCanada's Incentive Settlement can be found in Chapter 4 of the Board's RH-2-95 Summary.

Chapter 3

Revenue Requirement

The Net Revenue Requirement for toll design and cost allocation purposes approved for TransCanada for the 1997 Test Year is \$1,704,304,000 subject to any changes that may result from decisions taken by the Board in these Reasons. A summary of this revenue requirement is provided in Table 3-1.

Table 3-1
Transportation Revenue Requirement for the 1997 Test Year
(\$ 000)

	Application	NEB Adjustments	Authorized by NEB
Incentive Cost Envelope	689,839	-	689,839
Flow-Through Cost Envelope			
Income Taxes	102,106	-	102,106
Depreciation	252,230	-	252,230
Return	731,574	-	731,574
Foreign Exchange Cost	2,643	-	2,643
Electric Fuel Costs - Additional Units	12,680	-	12,680
Insurance Deductible Costs	3,701	-	3,701
Stress Corrosion Cracking & Corrosion Control	64,072	-	64,072
Sub Total Flow-Through Envelope	1,169,006	-	1,169,006
Regulatory Amortizations	(67,645)	-	(67,645)
Pressure Charges	4,854	-	4,854
Gross Revenue Requirement	1,796,054	-	1,796,054
Non-Discretionary Miscellaneous Revenue	(54,115)	-	(54,115)
Discretionary Miscellaneous Revenue	(12,300)	-	(12,300)
Interim Revenue Adjustment	(25,335)	-	(25,335)
Net Revenue Requirement	1,704,304	-	1,704,304

During the RH-1-97 proceeding, parties were afforded the opportunity to comment on TransCanada's 1997 Tolls Application and revisions. No parties filed comments on any aspect of TransCanada's Application with the exception of Consumers' complaint with respect to TransCanada's allocation units.

3.1 Incentive Cost Envelope

TransCanada included an amount of \$689,839,000 in its Incentive Cost Envelope for the 1997 Test Year. TransCanada indicated that this amount was determined by applying the 1997 Net Adjustment Factor of 102.75%, as defined in Article 2 of the Incentive Settlement, to its 1996 actual Incentive Envelope Costs excluding TBO and Foreign Exchange on Great Lakes payments. TransCanada's Incentive Settlement states that, subject to the specific adjustments and qualifications relating to TBO Costs and Municipal and Other Taxes set out in Articles 5 and 6 respectively of the Incentive Settlement, any variances between the actual costs contained in the Incentive Cost Envelope and the corresponding items in the Test-Year Costs shall be shared equally by TransCanada and its shippers. One half of such cost variance shall be recorded in an Incentive-Based Deferral Account and applied to the Cost of Service in the year immediately following the Test Year. The balance of the variance shall accrue to TransCanada as Incentive Revenue.

Decision

Although the Incentive Settlement does not contemplate specific Board approval of the costs contained within the Incentive Cost Envelope, the Board nevertheless accepts the amount of \$689,839,000 for toll making purposes for the 1997 Test Year.

3.2 Flow-Through Cost Envelope

TransCanada forecast items contained within the Flow-Through Cost Envelope to be \$1,169,006,000 for the 1997 Test Year. Section 1.8 (i) of TransCanada's Incentive Settlement contemplates that the Board will review and approve the reasonableness of the forecast of items covered in the Flow-Through Cost Envelope. In this regard, the components of TransCanada's rate of return on rate base are discussed further in Chapter 6 and TransCanada's approved Schedule of Flow-Through Income Taxes is provided in Appendix III.

Decision

The Board approves TransCanada's forecast of its Flow-Through Cost Envelope of \$1,169,006,000 for the 1997 Test Year.

3.3 Regulatory Amortizations

The disposition of the balances included in all deferral accounts in Regulatory Amortizations results in a reduction of \$67,645,000 to TransCanada's Net Revenue Requirement in the 1997 Test Year. Section 1.8 (iv) of TransCanada's Incentive Settlement provides that the Board will review and adjudicate on the disposition of Flow-Through Deferral Accounts pursuant to Section 8.5 and rule on any complaints filed in connection with such matter. Section 8.5 of TransCanada's Incentive Settlement states:

Information with respect to all variances and Non-Routine Adjustments to be recorded in Flow-Through Deferral Accounts in accordance with the terms of this Settlement

will be provided to the Tolls Task Force by TransCanada on or before 1 March of each year. In the event that the Tolls Task Force cannot, for any reason, agree on the disposition of these Flow-Through Deferral Account balances by 31 March of such year, such balances shall be applied to the Cost of Service in the current Test Year. Notwithstanding the foregoing, on or before 15 April of such Test Year, any shipper may file a complaint with the NEB regarding the disposition of all or any such Flow-Through Deferral Account balances. Any complaint must also contain a request by the shipper to make TransCanada's tolls interim effective 1 April pending the resolution by the NEB of the complaint.

There were no complaints received with respect to this provision. In TTF Resolution 98-13, the TTF examined the 1996 Test-Year Actual costs and agreed that the balances of the Flow-Through Deferral Account shall be applied to the Cost of Service in the 1997 Test Year. The Board approved this resolution on 8 May 1997.

Decision

The Board accepts the Total Regulatory Amortizations amount of \$67,645,000 for toll making purposes for the 1997 Test Year.

3.4 Non-Discretionary Miscellaneous Revenue

TransCanada's forecast of Non-Discretionary Miscellaneous Revenue for the 1997 Test Year was \$54,115,000. Section 9.1 of TransCanada's Incentive Settlement states:

Non-Discretionary Miscellaneous Revenue shall be forecast by TransCanada and approved by the NEB for each Test Year during the term of this Settlement and applied in the determination of the Net Revenue Requirement for toll making purposes in the applicable Test Year.

Decision

The Board approves TransCanada's Non-Discretionary Miscellaneous Revenue forecast of \$54,115,000 for the 1997 Test Year.

3.5 Discretionary Miscellaneous Revenue

Section 15.1 of TransCanada's Incentive Settlement establishes that Base Discretionary Miscellaneous Revenue shall be set at \$12,300,000 for the term of this Settlement, subject to adjustments in certain circumstances. For the 1997 Test Year, TransCanada used the base figure of \$12,300,000.

Decision

Although the Incentive Settlement does not contemplate specific Board approval of the forecast of costs for Discretionary Miscellaneous revenue, the Board accepts

TransCanada's base figure of \$12,300,000 for the 1997 Test Year for toll making purposes.

3.6 Interim Revenue Adjustment

In its revised interim tolls effective 1 May 1997, TransCanada included a forecast Interim Revenue Adjustment of \$25,335,000 which was calculated in accordance with Section 17.3 of the Incentive Settlement. This adjustment represents the total variance¹ for the period, 1 January 1997 to 30 April 1997, in which interim tolls were in effect. The Interim Revenue Adjustment plus carrying charges was amortized over the remaining months of the Test Year and applied to the Cost of Service to determine the Net Revenue Requirement in this Application. An annual rate of 4% was used to calculate carrying charges. The Board notes that Section 7.5 of these Reasons for Decision discusses the treatment of any further Interim Revenue Adjustment which may be required as a result of the Board's Decisions.

Decision

The Board accepts, subject to Section 7.5 of these Reasons for Decision, the Interim Revenue Adjustment of \$25,335,000 for the 1997 Test Year for toll making purposes.

3.7 Revisions to TransCanada's 1997 Tolls Application

By letter dated 29 April 1997, TransCanada filed proposed revisions to its 1997 Tolls Application to reflect three significant events. The first event was a decrease in its forecast 1997 TBO cost to remove a contract for 2 210 10³m³/d, after TransCanada had determined the contract, which had been anticipated at the time of the original application, would not be executed. The second event related to two TTF Resolutions which removed the cap on Interruptible Service ("IT") bidding and increased the Short Term Firm Transportation ("STFT") Service bid cap to four times the 100 percent load factor toll to Philipsburg less the East/West differential where applicable. The third event reflected an additional resolution by the TTF approving an incremental forecast cost of \$17.4 million, associated with TransCanada's Enhanced 1997 Pipeline Maintenance Program. No comments were received on any of these revisions.

Decision

The Board approves the matters contained in the revision dated 29 April 1997 to TransCanada's 1997 Tolls Application.

¹ The variance of \$25,335,000 results from the difference between the interim tolls which were in effect from 1 January 1997 to 30 April 1997, and the revised interim tolls effective 1 May 1997.

Chapter 4

Rate Base

Section 16.1 of the Incentive Settlement provides that a forecast of Rate Base will be submitted in support of TransCanada's annual tolls application for Board approval. A summary of TransCanada's applied-for Rate Base for the 1997 Test Year is provided in Table 4-1.

Table 4-1
Rate Base for the 1997 Test Year
(\$ 000)

	Application	NEB Adjustments	Authorized by NEB
Utility Investment			
Gross Plant	9,784,091	-	9,784,091
Accumulated Depreciation	<u>(2,479,335)</u>	-	<u>(2,479,335)</u>
Net Plant	7,304,756	-	7,304,756
Contributions in Aid of Construction	<u>(2,410)</u>	-	<u>(2,410)</u>
Total Plant	7,302,346	-	7,302,346
Working Capital			
Cash	22,243	-	22,243
GST Receivable, Net	2,320	-	2,320
Materials & Supplies	43,866	-	43,866
Transmission Linepack	39,905	-	39,905
Prepayments & Deposits	<u>1,428</u>	-	<u>1,428</u>
Total Working Capital	109,762	-	109,762
Deferred Costs			
Miscellaneous Deferred Items	37,797	-	37,797
Operating & Debt Service Deferrals	(33,211)	-	(33,211)
Surplus Pension	<u>10,450</u>	-	<u>10,450</u>
Total Deferred Costs	<u>15,036</u>	-	<u>15,036</u>
Total Rate Base	7,427,144	-	7,427,144

Decision

The Board approves TransCanada's applied-for Rate Base of \$7,427,144,000 for the 1997 Test Year.

Chapter 5

Deferral Accounts

TransCanada requested the continuation throughout the 1997 Test Year of all deferral accounts which were contemplated under Section 20.4 of the Incentive Settlement.

Decision

The Board approves the continuation throughout the 1997 Test Year of all deferral accounts which were contemplated under Section 20.4 of the Incentive Settlement.

Chapter 6

Cost of Capital

An adjustment mechanism for determining the annual approved rate of return on common equity as well as the appropriate capital structure, including the preferred share component, were matters which the Board considered and determined in the RH-2-94 proceeding. TransCanada's Incentive Settlement incorporated the relevant decisions from that proceeding. The Board's approved rate of return on common equity for the 1997 Test Year, pursuant to the adjustment mechanism approved in RH-2-94, and in accordance with amendments set out in the Board's letter dated 14 March 1997, is 10.67%. This approved rate of return is 58 basis points lower than the 11.25% rate approved for 1996. TransCanada incorporated the deemed common equity ratio of 30% approved in RH-2-94 in calculating its proposed 1997 tolls.

TransCanada applied for a rate of return on rate base of 9.85% for the 1997 Test Year, 58 basis points lower than the approved rate of 10.43% for 1996. TransCanada's applied-for deemed average capital structure and rates of return are shown below in Table 6-1 and discussed in further detail in sections 6.1 to 6.7.

Table 6-1
Deemed Average Capital Structure and
Rates of Return for the 1997 Test Year

	Amount (\$ 000)	Capital Structure (%)	Cost Rate (%)	Cost Componnet (%)
Funded Debt	4,182,574	54.70	10.09	5.52
Unfunded Debt	<u>439,136</u>	<u>5.75</u>	6.91	<u>0.40</u>
	4,621,710	60.45		5.92
Junior Subordinated Debentures	218,082	2.85	8.57	0.24
Preferred Share Capital	512,649	6.70	7.28	0.49
Common Equity	<u>2,293,903</u>	<u>30.00</u>	10.67	<u>3.20</u>
Total Capitalization	7,646,344¹	100.00		
Rate of Return on Rate Base				9.85

¹ Rate Base \$7,427,144 + GPUC \$219,200 = Total Capitalization \$7,646,344.

6.1 Funded Debt

TransCanada's funded debt represents the average principal of debt capital associated with the utility investments projected to be outstanding during the 1997 Test Year. TransCanada's funded debt is comprised of bonds, debentures and medium-term notes with varying maturities. These debt instruments are denominated in Canadian and foreign currencies.

TransCanada applied for an average funded debt amount of \$4,182,574,000 at a cost rate of 10.09%. The funded debt balance accounts for 54.70% of the applied-for deemed average capitalization for the 1997 Test Year.

Decision

The Board approves TransCanada's applied-for funded debt amount of \$4,182,574,000 at a cost rate of 10.09% for the 1997 Test Year.

6.2 Unfunded Debt

Unfunded debt represents that portion of TransCanada's capital structure which remains to be raised by long-term financing. The average unfunded debt balance, for the 1997 Test Year, is derived by subtracting the average funded debt, junior subordinated debentures, preferred share and common equity capital from the total average capitalization.

TransCanada applied for an average unfunded debt amount of \$439,136,000 at an average cost rate of 6.91%. This unfunded debt rate was calculated according to the Board's approved methodology which is equivalent to the forecasted blend of short-term and long-term financing costs.

Decision

The Board approves an unfunded debt amount of \$439,136,000 at a cost rate of 6.91% for the 1997 Test Year.

6.3 Junior Subordinated Debentures

TransCanada applied for a Junior Subordinated Debenture amount of \$218,082,000 at an average cost rate of 8.57% for the 1997 Test Year. TransCanada noted that although the Junior Subordinated Debentures are debt instruments, they were issued by TransCanada as a cost-effective alternative to preferred shares. TransCanada views these securities as comprising a portion of the preferred equity component of its regulated capitalization.

Decision

The Board approves a Junior Subordinated Debenture amount of \$218,082,000 at a cost rate of 8.57% for the 1997 Test Year.

6.4 Preferred Shares

TransCanada's deemed average capitalization includes a preferred share amount of \$512,649,000 at an average cost rate of 7.28% for the 1997 Test Year. The inclusion of a preferred share component in TransCanada's deemed capital structure is consistent with the Board's decision in the RH-2-94 proceeding to allow TransCanada to maintain preferred shares in its capital structure.

Decision

The Board approves TransCanada's applied-for preferred share amount of \$512,649,000 at an average cost rate of 7.28% for the 1997 Test Year.

6.5 Common Equity Ratio

TransCanada's applied-for deemed capital structure incorporates a common equity ratio of 30% as approved by the Board in its RH-2-94 Decision.

6.6 Rate of Return on Common Equity

TransCanada used a rate of return on common equity of 10.67%. This rate of return on common equity was approved by the Board on 14 March 1997.

6.7 Rate of Return on Rate Base

Decision

The Board approves a rate of return on rate base of 9.85% for TransCanada for the 1997 Test Year. The approved deemed capital structure and overall rate of return for the 1997 Test Year is as shown in Table 6-1.

Chapter 7

Toll Design and Tariff Matters

7.1 Forecast of Aggregate Contract Demand

Section 16.1 of TransCanada's Incentive Settlement specifies that TransCanada's forecast of aggregate contract demand shall be submitted to the NEB for approval. TransCanada's forecast of aggregate contract demand for the 1997 Test Year was $68\,333\,10^6\text{m}^3$ (2,412 Bcf) of which $33\,240\,10^6\text{m}^3$ (1,173 Bcf) was forecast for the domestic market and $35\,093\,10^6\text{m}^3$ (1,239 Bcf) was forecast for the export market.

Decision

The Board accepts TransCanada's 1997 forecast of aggregate contract demand for toll design and cost allocation purposes.

7.2 Allocation Units Issue

TransCanada explained that it currently allocates its Cost of Service among its five domestic toll zones through the use of both volume and volume-distance allocation units. The allocation units issue raised by Consumers in its letter dated 30 April 1997, pertains to the volume-distance aspect of cost allocation; specifically the calculation of the load centres for distributor delivery areas ("DDA's"). A load centre, expressed in kilometres from Empress, Alberta, represents the volume-weighted average distance of haul for deliveries to a DDA during the most recent calendar year ("base year"). In the process of determining allocation units, load centre kilometres are multiplied by the volume of gas forecast to be delivered in the Test Year for each of the DDA's within each domestic toll zone. By way of example, there are nine DDA's in TransCanada's Eastern Toll Zone. The products are then totalled for each toll zone to determine the total volume-distance allocation units for that zone.

Currently, TransCanada uses metered volumes to calculate the load centre for each DDA. In TransCanada's view, the use of metered volumes reflects the actual utilization of its system to each location within a delivery area. TransCanada maintained that this methodology reflects actual delivery patterns on the system, is objective (as volumes are known and measurable), and is simple to understand. TransCanada also submitted that the volume-distance allocation units reflect the "user-pay" principle; this means that shippers moving the greatest volumes of gas over the longest distance pay the greatest proportion of the costs of the system. TransCanada stated that it has no financial interest in the issue raised by Consumers, but rather its position is to ensure that the methodology used to allocate costs is the fairest for all shippers.

In discussions with Consumers prior to the commencement of the hearing regarding the allocation units issue, TransCanada determined that certain assumptions which it had been using for storage volumes were incorrect. As a result, TransCanada proposed revisions to the methodology for determining the volumes at Dawn and Parkway which are used in the load centre calculations. For the load centre calculations contained in the original filing of the application, TransCanada had assumed

that all STS injection volumes were returned to TransCanada's system upon withdrawal from storage. Based on this assumption, storage injection volumes were not included at the point of injection and storage withdrawal volumes were not included at the point of withdrawal. All storage volumes were assumed to be accounted for at the final delivery location. It was later determined that this assumption was not valid, as not all STS volumes injected into storage are returned to TransCanada's system. As a result, TransCanada stated that they needed to find a methodology which would capture in the load centre calculations, STS volumes which do not re-enter its system. TransCanada maintained that they achieved this objective by using metered volumes without further adjustments.

TransCanada therefore requested the Board's approval for a revised methodology to reflect metered volumes at Dawn-Consumers and Parkway-Consumers, and metered volumes less TransCanada's M12 or C1 nominations at Dawn-Union and Parkway-Union. TransCanada explained that, since Dawn and Parkway function as both receipt and delivery points, metered volumes at these two points reflect deliveries net of receipts. TransCanada maintained that double counting does not occur, and that its proposed modification reflects the actual utilization of TransCanada's system for both transactions. In this regard, TransCanada noted that STS injection volumes are counted as a delivery at the point of injection, STS withdrawal volumes are counted as a receipt at the point of withdrawal, and the volumes withdrawn from storage which return to TransCanada's system are counted as a delivery at the final delivery location.

During the hearing, TransCanada also requested the Board's approval to correct an error in the calculation of the Gaz Métropolitain Eastern Delivery Area ("EDA") load centre. TransCanada noted that Sabrevois is both an export point on its system, and a domestic delivery point in the Gaz Métropolitain EDA, and that both domestic and export volumes at Sabrevois had been erroneously included in the calculation of the Gaz Métropolitain EDA load centre. TransCanada explained that there is only one meter at Sabrevois through which both domestic and export volumes flow and that for load centre calculation purposes domestic and export volumes should be separated, based on invoiced volumes. It was further noted that this same error had also occurred for Spruce, Manitoba and at Dawn-Export, and that further revisions would be required to correct the volumes used at these points in the load centre calculations. TransCanada added that an adjustment based on invoiced volumes is appropriate for those locations where both export and domestic volumes flow through the same meter.

With respect to the methodology for calculating load centres, Consumers argued that the "as-billed" method should be used instead of metered volumes and requested that the billed-volume approach be applied to all domestic shippers. Consumers stated that volumes should track billings because that is what shippers are paying for. While agreeing that TransCanada's method of using metered volumes captures the delivery patterns on its system during the Base Year, Consumers submitted that it does not capture the as-billed pattern; nor does it reflect the costs incurred, to the extent that diversions occur. In its view, the as-billed approach better reflects "user-pay" as those volumes would be reflected in the load centre for which the volumes are billed. Consumers added that, as a result of TransCanada's method, the shipper's "home" delivery area does not get credit for billed volumes for the purposes of cost allocation in relation to load centres. Consumers claimed that the as-billed approach aligns the billing process and the cost allocation process, including the calculation of load centres, while the metered-volume approach does not. Consumers suggested that the as-billed method is objective, captures STS injection volumes when they leave and re-enter the system, will not result in double counting of STS volumes, and is simpler to understand than the metered-volume method.

Consumers supported the proposed correction to the volumes at Sabrevois, Dawn-Export and Spruce, and added that this technique of "splitting the meter" could be used to break out metered volumes at points such as Parkway-Union and Dawn-Union, and could be used to distinguish between deliveries to Union Central Delivery Area ("CDA") shippers and Consumers CDA shippers at those points.

Union/Centra supported Consumers' position in final argument and adopted Consumers' reasoning for that position. Union/Centra stated that because of the configuration of the systems of TransCanada, Consumers and Union, some of Consumers' deliveries are metered in the Union CDA at Parkway. These volumes then go into storage and are later delivered to the Consumers CDA, via Union's system, without having returned to TransCanada's system. Union/Centra explained that Consumers' deliveries to Union-Parkway travel no farther on TransCanada's system than those to Consumers-Parkway, and that Consumers is invoiced for deliveries to its franchise area in both cases. Union/Centra added that cost causation should prevail over an artificial distinction, and for load centre purposes, the gas should be assumed by TransCanada as having been delivered to the Consumers' franchise area in the CDA at Parkway.

TransCanada responded that shipper-specific delivery information by delivery point for every shipper does not exist. TransCanada explained that it cannot distinguish ownership of certain volumes, which could belong to more than one shipper, that are delivered at a particular meter. TransCanada added that it is able to track nominations to the appropriate delivery area, but the actual deliveries made to the meters within that delivery area are determined by the distributor.

In regard to Union/Centra's argument that the gas going into storage eventually reaches Consumers' franchise area, TransCanada replied that these volumes use another system to get to that market and that TransCanada does not know what happens to the gas on the downstream side of its meter. TransCanada added that since some of the STS withdrawal volumes enter Consumers' market area directly from Union's system and do not re-enter TransCanada's system, it would be incorrect to assume that the gas used TransCanada's system to get to Consumers' market.

Views of the Board

At the conclusion of the proceeding, the Board had for consideration two approaches for calculating distributor load centres: TransCanada's metered-volume method and Consumers' as-billed approach. The Board is of the view that the metered-volume method is fair, objective and easy to understand and reflects the actual delivery patterns on TransCanada's system in the calculation of the distributor delivery area load centres.

With respect to the as-billed method, the Board is concerned that the potential effects on cost allocation of using this approach to calculate load centres are unknown. The Board notes that when load centres based on metered volumes are used in the calculation of allocation units, the resulting cost allocation has, in the past, been accepted as fair and has resulted in what have been considered as just and reasonable tolls. The Board further notes that, based on previous experience, there is a high level of certainty as to the impact of the metered-volume methodology on the allocation of costs. As a result, the Board is not persuaded that the billed-volume approach would result in a fairer allocation of costs, nor that it is necessary to change the current methodology at this time.

The Board is not persuaded that the as-billed method results in a more objective representation of delivery patterns or is as simple and easy to understand as the metered-volume approach. The Board also notes TransCanada's position that shipper-specific delivery information for each delivery point is not available. The Board, therefore, is not convinced that there is, in any event, sufficient information available to calculate shipper-specific load centres.

The Board notes that Consumers did not file written evidence or produce witnesses for cross-examination during the hearing. As a result, the Board and other parties, including the Applicant, were unable to adequately test Consumers' position regarding the use of billed volumes in the calculation of load centres. The Board is of the view that Consumers also did not, in cross-examination or argument, raise sufficient doubt as to the appropriateness of TransCanada's current metered-volume approach to warrant a change in methodology at this time.

With respect to Union/Centra's position, first expressed in final argument, regarding cost causation and its belief that TransCanada's methodology is artificial, the Board notes that Union/Centra also did not provide evidence or witnesses in support of this position.

In regard to TransCanada's proposed revisions to the methodology used to determine the volumes at Dawn and Parkway which are used in the load centre calculations, the Board is satisfied that the proposed revisions are appropriate and that, as a result, double counting of STS volumes will not occur.

The Board finds that the use of invoiced volumes to split the meter is appropriate in order to allocate volumes only at meters through which both domestic and export volumes flow; that is, Sabrevois, Dawn-Export and Spruce. The Board accepts TransCanada's view that the use of invoiced volumes to segregate domestic and export volumes, for the purposes of the load centre calculations, is a separate and distinct issue from that raised by Consumers. The distinction is that domestic and export volumes are thereby segregated and customer-specific volumes are not reflected in the determination of the load centres.

Decision

The Board approves the continued use of metered volumes to calculate the load centres for DDA's. The Board also approves TransCanada's proposed revisions to the methodology for capturing STS volumes which are used in the load centre calculations as well as TransCanada's proposed changes at Sabrevois, Dawn-Export and Spruce. The Board directs TransCanada to reflect these decisions when filing its Compliance Tolls.

7.3 FST Conversion Issue

7.3.1 Background

Description of FST

FST is an annual service, as opposed to a daily service, such as Firm Transportation. For FT service, shippers provide TransCanada with a daily nomination of the volume to be transported and the locations to which it is to be transported, within their contractual rights. Delivery obligations are determined within established tolerances on a daily and seasonal basis. By contrast, for FST service, TransCanada each day tenders a variable portion of a shipper's annual contract quantity to be transported, within certain parameters, from Empress. The FST shipper then nominates back to TransCanada, the volume it will accept for that day.

FST shippers must be able to accommodate daily variances in transportation volumes tendered by TransCanada. Accordingly, they must have access to storage at the downstream end of the system. Similarly, at the upstream end, FST suppliers must be able to accommodate fluctuating quantities of gas for transportation.

FST shippers receive the benefit of a reduced toll (a differential/[discount] from the FT service toll) which is intended to reflect the costs they incur to cope with the variable deliveries. For TransCanada, FST provides an important degree of flexibility in both design and operation of the system. TransCanada also uses FST to minimize the impact of volume fluctuations on all other shippers, from planned and unplanned maintenance and outages.

Pricing of FST

In each of the years from 1973 through 1994, the price for FST was approved based on a discount from the firm service price. The FST differential was based on an estimate of what it would cost TransCanada to convert the FST delivery pattern to an FT service delivery pattern if it were to contract for storage and transportation service. This was referred to as the "avoided cost methodology".

The original FST differential was based solely on transportation and storage costs in Ontario (the "downstream differential"). In 1989, the Board approved an upstream component of the differential which normally was reimbursed to the FST supplier.

RH-3-94 Suite of Services FST Differential Methodology

In the 1995 TransCanada rate hearing (RH-3-94), CAPP proposed a change in the way FST should be priced. CAPP proposed a "suite of services" methodology and suggested that instead of estimating what it would cost TransCanada to convert FST to FT service, the FST toll should be calculated as if it were a combination of existing services to approximate the FST delivery pattern. The differential would then be the difference between the cost of FT service and the cost of the suite of services.

The Board approved CAPP's proposal which resulted in the level of the FST differential being reduced from 38¢/GJ to 14¢/GJ. In addition, the upstream component of the FST differential was eliminated.

Exercise of FST Conversion Options

As result of the RH-3-94 decision, both Consumers and Union exercised their right to convert from FST to FT service by giving three years' notice. Effective 1 November 1998, both companies are scheduled to convert two-thirds of their annual contract quantity to FT service. Consumers has also given notice to convert its remaining one-third effective 1 November 1999. On 31 October 1996, Union gave notice to convert a portion of its remaining FST volumes effective 1 November 1999.

In summary, it is anticipated that 150 Bcf of FST will be converted as of 1 November 1998 and 14.6 Bcf as of 1 November 1999. The only FST which is expected to remain on TransCanada's system after 1 November 1999 is a volume of 29.2 Bcf held by Union.

RH-2-95 FST Settlement Agreement

In the fall of 1995, TransCanada facilitated discussions between FST shippers and CAPP which led to a one-year agreement regarding the FST differential. The parties agreed to a refinement to the suite of services calculation for the FST differential in order to better reflect the use of discretionary services on the TransCanada system and the split of the FST differential between upstream and downstream components. The resulting FST Agreement provided for a 25¢/GJ differential which was split 21¢/GJ downstream and 4¢/GJ upstream.

In light of the conversion notices, it was proposed that TransCanada and its shippers would implement a consultative process with the objective of identifying ways and means of maintaining and possibly enhancing on a long-term basis, the operating flexibility currently provided by the service characteristics of FST in the most cost-effective manner.

FST Conversion Process

Accordingly, during the first quarter of 1996, TransCanada in collaboration with a committee of its shippers (the "Committee") studied various alternatives to provide comparable system flexibility to that afforded by FST. Based on a number of factors, the Committee determined that the appropriate method of replacing FST would be to hold an open-bid process for the provision of services. In May 1996, TransCanada prepared an FST replacement Request for Proposal ("RFP") and distributed it in the gas industry.

Four RFP options were identified¹ and the RFP was sent to approximately 75 companies that were considered to be prospective suppliers of such services as storage, load balancing, and alternative transportation. Proposals were received and evaluated during July and August 1996 on the basis of objective criteria established by TransCanada. TransCanada then approached individual companies and negotiated contracts.

In addition to evaluating the proposals received, TransCanada examined the option of providing the required flexibility by adding pipeline facilities but concluded that this option, either as a separate option or in combination with other proposals, was not the most cost-effective solution. Based on its

¹ The four options were: Variable Firm Transportation Service; Firm Service Tendered; Storage Service; and Load Balancing Service. In addition, proposals for other services which could satisfy the requirements were also encouraged by TransCanada to be submitted.

evaluation and follow-up efforts, TransCanada selected a storage-based solution for transporting on an FT basis the gas volumes previously contracted for at FST rates.

7.3.2 Filing of Adequate Information

An issue relating to whether or not the applicant had filed adequate information regarding unsuccessful bids was raised during the proceeding.

Union/Centra submitted that the information which TransCanada filed concerning the bids it received from suppliers of potential FST substitute services, but that were not selected, was inadequate to allow an independent assessment by the Board or interested parties that TransCanada has picked the best combination of options available to it. Union/Centra indicated that the regulatory process has considered it appropriate, in the past, to have the Board and interested parties examine the information on which TransCanada exercises its judgement and to form their own judgements on the prudence or reasonableness of TransCanada's decision. At a minimum, Union/Centra suggested that the Board could require TransCanada to file with the Board, in confidence, a summary of each unsuccessful bid, together with an explanation of why the bid, either by itself, or in combination with others, did not constitute the best, or a part of the best, conversion services.

Consumers was somewhat concerned with the limited amount of information on other bids. It suggested that, in the future, greater disclosure could assure all interested parties that the public record is adequate for decision-making purposes.

TransCanada submitted that it had provided adequate information in light of requested confidentiality concerns of parties. TransCanada provided a summary of the bids which demonstrated the range of bids that had been received. In addition, it responded during cross-examination with further details regarding the selection of a short list of bidders, primarily on the basis of cost and flexibility.

In reply argument, TransCanada asked the Board to consider TransCanada's commitment to discuss future bidding for FST conversion with shippers prior to imposing guidelines.

Views of the Board

In reaching its decision on any issue before it, the Board must form its own conclusion based on the evidence adduced during the proceeding. It is not sufficient for the Board to accept the position of an applicant solely on the basis of the applicant's assurances that approval of its application is in the public interest or results in just and reasonable tolls. However, the nature and quantity of evidence will vary from proceeding to proceeding and, ultimately, the Board must exercise its discretion, as an expert tribunal, in determining whether the evidence is sufficient to allow the Board to take its decision.

With respect to the evidence before it relating to TransCanada's FST Conversion proposal, the Board notes the following:

- TransCanada consulted with industry on the bidding process;
- the bidding process was open;

- the successful package was approximately \$5 million less than the next lowest bid which did not provide the same level of operating flexibility;
- detailed information regarding the successful bids was submitted by TransCanada;
- summaries of unsuccessful bids were presented, albeit with regard given to keeping confidential commercially sensitive information; and
- the contracts resulting from the bidding process will be held with parties at arm's length to TransCanada.

The Board is of the view that there was sufficient information placed on the record to make a determination that TransCanada had conducted the FST conversion process in a prudent and objective manner. Further, the Board does not believe that a review of further details of the unsuccessful bids would add materially to its ability to reach a decision on the merits of TransCanada's application.

The Board notes TransCanada's commitment to retain the information on FST conversion bids for a minimum period of two years. Accordingly, the Board has the opportunity to examine this information in the course of a future audit of TransCanada.

7.3.3 FST Conversion Proposal

The FST Conversion proposal includes a combination of storage, balancing and transportation contracts as well as the purchase of start-up gas to replace 150 Bcf of FST with FT service effective 1 November 1998.

Components of FST Conversion Proposal

AEC was selected to provide the upstream storage and ANR the downstream storage. In TransCanada's opinion, the flexibility provided by this storage, while not identical to that provided by FST, will be comparable.

In addition to the storage arrangements, TransCanada has entered into a gas balancing arrangement with NOVA to accommodate the use of upstream storage. Included in the arrangements with ANR are downstream transportation services on Great Lakes.

TransCanada will also require additional Firm Service capacity on Union's system together with some related facilities additions on its Dawn Extension. These additional facilities will be considered in the TransCanada GH-2-97 facilities proceeding.

Finally, TransCanada will also purchase start-up gas to be placed in downstream storage in order to ensure from the outset that it has the operational flexibility to perform scheduled maintenance and to protect against unplanned outages.

The estimated annual cost of the FST conversion is \$41.8 million compared with the cost of the current FST differential, in terms of the discount from FT, of \$41.3 million.

Position of TransCanada

TransCanada argued that its FST Conversion proposal is reliable, efficient and cost effective. In its view, this proposal will allow TransCanada to maintain the level of flexibility that the Company requires to operate its system effectively and result in a minimal impact on tolls.

Position of Intervenors

CAPP requested that the Board approve TransCanada's FST Conversion proposal on the basis that the process involved extensive industry discussions and that the proposal was determined through a competitive bidding process. CAPP also noted that this proposal provides comparable flexibility to FST at the lowest possible cost.

Consumers supported the storage proposal on the basis of its comparable level of flexibility, its apparent reliability and the reasonableness of cost estimates.

The ADOE supported the approval of TransCanada's FST Conversion proposal on the basis that it is a reasonable proposal designed to maintain operational flexibility at a reasonable cost.

Union/Centra neither supported nor opposed the TransCanada proposal but indicated that it supported the process utilized by TransCanada to solicit a package of services to replace FST.

Views of the Board

The Board is of the view that the process utilized by TransCanada to obtain proposals to replace FST with a package of services based on storage was prudent, cost-effective and objective. The Board is also of the view that the FST Conversion proposal will provide a level of flexibility comparable to that provided by the FST it will replace.

The Board accepts the evidence from TransCanada regarding the selection of winning bids according to objective criteria.

The Board notes that TransCanada's Incentive Settlement contains provisions which provide the framework for shippers and TransCanada to examine the impact of FST conversion.

Decision

The Board approves TransCanada's proposal to replace FST with FT service by entering into a combination of storage, balancing and transportation arrangements, and by purchasing start-up gas.

The Board approves the specific contractual arrangements that TransCanada has entered into with AEC, ANR, Great Lakes, and NOVA, subject to these agreements receiving other necessary regulatory approvals.

In accordance with Section 5.1 of the Incentive Settlement, the Board also approves the contracting by TransCanada of an additional 412 MMcf/day of M12 capacity on Union's system for the purposes of FST conversion.

TransCanada had requested that the Board approve TransCanada's plan to enter into a consultative process with its shippers to map out the tolling consequences of the new service proposed to replace FST. The Board commends TransCanada's intention to consult with its shippers but notes that the Incentive Settlement provides the framework for such a process. Accordingly, the Board does not consider a decision necessary in this regard.

7.4 Great Lakes Refund

On 19 September 1996, the Board issued its decision on how TransCanada should distribute a refund of approximately US\$38 million which it expected to receive from Great Lakes over a period of three years commencing in 1996. The refund related to excess incremental rates paid by TransCanada to Great Lakes for service during the period 1 November 1991 to 30 September 1995.

In a letter dated 18 November 1996, TransCanada indicated that events in the United States had created a concern that it may not be appropriate to unconditionally credit all amounts refunded to its shippers. TransCanada noted that various parties in the United States had appealed the FERC Orders which gave rise to the refunds to the U.S. Court of Appeals. The petitions for review related to both the FERC's substantive finding in favour of rolled-in rates and its refund/surcharge remedy. TransCanada further noted that the granting of these appeals could result in Great Lakes being required to retroactively recover the amount of the refund from its shippers, with the result that TransCanada would be looking to its shippers for recovery of these funds.

In this regard, the Board on 24 January 1997, approved TransCanada's request to make its 1996 FT, FST and STS tolls interim subject to the disposition of all appeals or any successor actions relating to the FERC Orders regarding incremental tolling on the Great Lakes system. In this proceeding, TransCanada noted that, as a result of the refund mechanism used by Great Lakes, smaller refund amounts are continuing to flow through TransCanada to its shippers during the 1997 Test Year. As a result, TransCanada asked the Board to extend the order made in the 24 January 1997 letter to its 1997 final tolls approved in RH-1-97.

The Board, in its letter dated 26 March 1997, asked parties to provide any comments they may have regarding this issue. No comments were received.

Decision

With respect to the Great Lakes Refund issue, the Board approves TransCanada's request to have its 1997 FT, FST and STS tolls remain interim subject to the disposition of all appeals relating to the relevant FERC Orders or any successor actions arising from the disposition of those actions including resulting FERC decisions.

7.5 Compliance Tolls

The Board notes that its approval of TransCanada's proposed changes for determining the volumes at Dawn and Parkway as well as TransCanada's corrections to the volumes at Sabrevois, Dawn-Export and Spruce, will affect load centre calculations. Consequently, the Board notes that final tolls may be somewhat different from TransCanada's currently approved interim tolls which might, therefore, impact TransCanada's Net Revenue Requirement for toll design and cost allocation purposes.

Decision

TransCanada is directed to file with the Board, forthwith, revised schedules and tolls implementing all decisions of the Board as well as TransCanada's proposed correction for allocating volumes between the export and domestic locations. TransCanada is directed to inform the Board and RH-1-97 Interested Parties as to how it wishes to proceed if, by implementing these decisions, any changes are required to the current interim tolls and supporting schedules.

The current interim tolls will remain in effect until the Board has issued its final tolls order with respect to 1997 tolls.

Chapter 8

Disposition

The foregoing chapters together with Order No. TG-4-97 constitute our Decision and Reasons for Decision on these matters.

J.A. Snider
Presiding Member

R. Priddle
Member

R.D. Revel
Member

Appendix I

Order TG-4-97

ORDER TG-4-97

IN THE MATTER OF the *National Energy Board Act* ("the Act") and the Regulations made thereunder; and

IN THE MATTER OF an application dated 19 March 1997, and amended 29 April 1997, by TransCanada PipeLines Limited ("TransCanada") pursuant to Part IV of the Act for certain orders respecting its tolls; filed with the National Energy Board ("the Board") under File No. 4200-T001-11; and

IN THE MATTER OF an application by TransCanada dated 6 May 1997 pursuant to sections 59 and 70 of the Act, for approval to enter into a combination of storage, balancing and transportation contracts, and to purchase "start-up" gas to replace most of its Firm Service Tendered ("FST") with Firm Transportation ("FT") Service effective 1 November 1998 ("FST Conversion proposal").

BEFORE the Board on 4 September 1997.

WHEREAS TransCanada filed an application dated 19 March 1997 and amended on 29 April 1997, for an order fixing just and reasonable tolls that it may charge for in respect of transportation services rendered effective 1 January 1997;

AND WHEREAS TransCanada filed an application dated 6 May 1997 for approval of its FST Conversion proposal;

AND WHEREAS the Board, on 20 December 1996, issued Order TGI-7-96 making TransCanada's tolls interim effective 1 January 1997, pending the Board's final decision on the Company's 1997 Tolls Application;

AND WHEREAS the Board, on 26 March 1997, issued Order AO-1-TGI-7-96 approving TransCanada's proposal for revised interim tolls effective 1 April 1997;

AND WHEREAS the Board, on 30 April 1997, issued Order AO-2-TGI-7-96 approving TransCanada's proposal for revised interim tolls effective 1 May 1997;

AND WHEREAS a public hearing pursuant to Hearing Order RH-1-97, as amended, was held in Calgary, Alberta during which time the Board heard the evidence and argument presented by TransCanada and all interested parties;

AND WHEREAS the Board's decisions on the Applications are set out in its Reasons for Decision dated September 1997, and in this Order;

IT IS ORDERED THAT:

1. TransCanada is directed to file with the Board, forthwith, revised schedules and tolls implementing all decisions of the Board as well as TransCanada's proposed correction for allocating volumes between the export and domestic locations.
2. If, by implementing these decisions, any changes are required to its current interim tolls and supporting schedules, TransCanada is directed to suggest to the Board and all interested parties how it wishes to proceed.
3. Order AO-2-TGI-7-96, which authorized TransCanada's tolls to be charged on an interim basis shall continue pending a final decision on the said Application.
4. The Board approves TransCanada's proposal to replace FST with FT service by entering into a combination of storage, balancing and transportation arrangements, and by purchasing start-up gas.
5. The Board approves the specific contractual arrangements that TransCanada has entered into with AEC, ANR, Great Lakes, and NOVA, subject to these agreements receiving other necessary regulatory approvals.
6. The Board also approves the contracting by TransCanada of an additional 412 MMcf/day of M12 capacity on Union's system for the purposes of FST conversion.

NATIONAL ENERGY BOARD

M. L. Mantha
Secretary

Appendix II

Key Provisions of TransCanada's Incentive Cost Recovery & Revenue Sharing Settlement

(Note: The information provided in this appendix is provided solely for the convenience of the reader and does not constitute part of the Decision or Reasons. The reader is referred to Chapter 4 of the Board's RH-2-95 Summary Document entitled "Compilation of Key Documents Related to the Board's RH-2-95 Decisions" wherein the complete text of TransCanada's Incentive Settlement was reproduced.)

The following is a summary of some of the key provisions of TransCanada's Incentive Settlement:

1. The Incentive Settlement covers a four-year period from 1 January 1996 to 31 December 1999.
2. The primary objectives of the Incentive Settlement are:
 - to more closely align the interests of the Parties by providing a framework which encourages efficiency gains, cost minimization and maximization of system utilization;
 - to provide for the lowest possible costs and the highest possible throughput without compromising pipeline efficiency and reliability or adversely impacting safety or the environment;
 - to result in tolls to shippers that will be lower than they otherwise would have been if determined under traditional cost of service regulation;
 - to maintain or improve the historic high level of service quality of the TransCanada system;
 - to maintain or improve the financial integrity of TransCanada;
 - to preserve firm shippers' flexibility and ability to fully utilize their transportation contracts. The service attributes of FT service such as diversions, single handshakes, assignments, capacity release and enhanced capacity release, each reflecting their current Transportation Tariff and TransCanada policy provisions, will be maintained or enhanced, subject to possible change by the Tolls Task Force and the NEB; and
 - to provide for the active management by TransCanada of its foreign exchange and debt management programs in order to minimize costs.
3. The Board's role regarding the implementation of the Incentive Settlement and the resulting calculation of tolls is:
 - review and approve the reasonableness of the forecast of items covered in the Flow-Through Cost Envelope;
 - adjudicate all disputes which arise out of the Incentive Settlement and which cannot be resolved amongst the Parties in accordance with the terms of the Incentive Settlement;
 - to be the arbiter of matters involving additions or changes to Rate Base;
 - to review and adjudicate on the disposition of Flow-Through Deferral Accounts pursuant to Section 8.5 and rule on any complaints filed in connection with such matter; and
 - generally fulfil its mandate as required under the Act.

It is acknowledged that the NEB will have exclusive jurisdiction over the establishment of TransCanada's tolls and that any matters respecting the derivation of tolls under the Incentive Settlement shall be determined by the NEB.

4. The Incentive Cost Envelope is made up of TBO Costs, OM&A Expense, Gas Related Expense, Municipal and Other Taxes, and NEB Cost Recovery Expense. Any variances between the annual Incentive Cost Envelope as calculated according to the Incentive Settlement and actual costs in the Incentive Cost Envelope during the year, will be divided 50/50 between TransCanada and its shippers.
5. The Flow-Through Cost Envelope is made up of the following components: Return on Rate Base, Income Taxes, Depreciation, Foreign Exchange on Debt Retirements, Foreign Exchange Costs, Insurance Deductible Costs, and SCC Costs. Any variances will be applied to TransCanada's Cost of Service in the following Test Year.
6. Unanticipated changes in certain costs (e.g. changes in revenues or expenses resulting from changes in applicable accounting standards - Canadian generally accepted accounting principles and Gas Pipeline Uniform Accounting Regulations) included in the Incentive Cost Envelope or in Discretionary Miscellaneous Revenue in any Test Year shall be treated as Non-Routine Adjustments and included in a Flow-Through Deferral Account and, subject to the review and complaint procedure set out in Section 8.5, be applied to the Cost of Service in the year immediately following the Test Year.
7. TransCanada's Rate Base will be determined in each Test Year and submitted to the Board for approval.
8. Depreciation Expense will be based on approved rates in effect at 31 December 1995 or those rates approved thereafter by the NEB.
9. Rate of Return means the sum of the weighted average cost of debt including funded and unfunded debt (approximately 60% of total capitalization), the weighted average cost of preferred stock (approximately 10% of total capitalization), and the return on equity (30% of total capitalization) as each applies to TransCanada. The return on equity shall be determined in accordance with the methodology established in the NEB's RH-2-94 Multi-Pipeline Cost of Capital proceeding.
10. Non-Discretionary Miscellaneous Revenue shall be forecast by TransCanada and approved by the NEB for each Test Year.
11. Discretionary Miscellaneous Revenue shall be established at a base level of \$12,300,000 for the term of the Incentive Settlement unless adjusted in certain circumstances. Any excess or shortfall from the base level shall be shared 1/3 by TransCanada and 2/3 by its shippers.

Appendix III

TransCanada's Schedule of Flow-Through Income Taxes for the 1997 Test Year (\$000)

	Application	NEB Adjustments	Authorized by NEB
Equity Component	274,062	-	274,062
Depreciation	252,230	-	252,230
Large Corporation Tax	18,347	-	18,347
Preferred Share Dividend Tax	215	-	215
Non-allowed Amortization of Debt Discount & Expense and Foreign Exchange Costs	5,708	-	5,708
Non-allowed Expenses	(1,057)	-	(1,057)
Capital Cost Allowance	(413,533)	-	(413,533)
Benefits Capitalized	(3,281)	-	(3,281)
Eligible Capital Expenses	(70)	-	(70)
Interest AFUDC	(14,177)	-	(14,177)
North Bay Litigation Costs	(4,768)	-	(4,768)
Issue Costs	(6,287)	-	(6,287)
Taxable Income	107,389	-	107,389
Taxes at $0.43756 \div (1-0.43756) \times$ Taxable Income	83,544	-	83,544
Recovery of Large Corporation Tax	18,347	-	18,347
Income Tax on Preferred Share Dividends	215	-	215
Utility Income Tax Requirement	102,106	-	102,106