

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE GAS DISTRIBUTION ACT

- and -

IN THE MATTER OF AN APPLICATION by **HERITAGE GAS LIMITED** requesting that the Board determine whether the prudently incurred costs of natural gas storage should be regulated by the Board and included with Heritage's cost of service

BEFORE: Peter W. Gurnham Q.C., Chair

APPLICANT: **HERITAGE GAS LIMITED**
John MacPherson, Q.C.

INTERVENORS: **ALTON NATURAL GAS STORAGE LP**
David Birkett

CONSUMER ADVOCATE
John Merrick, Q.C.
William L. Mahody, LL.B.

NOVA SCOTIA POWER INCORPORATED
Nicole Godbout, LL.B.

FINAL SUBMISSIONS: February 6, 2014

DECISION DATE: **February 20, 2014**

DECISION: The Board finds that the storage of natural gas is a related service under Section 22(1) of the *Gas Distribution Act* and the prudently incurred costs of natural gas storage may be included with Heritage's cost of service.

I INTRODUCTION

[1] On November 6, 2013, Heritage Gas Limited (“Heritage”) applied to the Nova Scotia Utility and Review Board (“Board”) with regard to the recovery of natural gas storage costs. Heritage requests a determination as to whether the prudently incurred costs of natural gas storage should be included with Heritage’s cost of service.

[2] The Board, by Order dated November 26, 2013, set the following timeline to apply to the proceeding:

Notices of Intervention	Monday, January 6, 2014
Information Requests (IRs) to Heritage	Monday, January 13, 2014
Responses to IRs from Heritage	Monday, January 20, 2014
Submissions from Interested Parties	Monday, February 3, 2014
Letters of Comment	Monday, February 3, 2014
Reply Submission by Heritage	Monday, February 10, 2014

[3] The following parties filed Notices of Intervention: Alton Natural Gas Storage LP (“Alton”); the Consumer Advocate (“CA”); and Nova Scotia Power Incorporated (“NSPI”).

[4] Information Requests (“IRs”) were submitted by the CA and responded to by Heritage. A submission was filed by the CA and letters of comment were filed by the Minister of Energy and Port Hawkesbury Paper LP (“PHP”).

II POSITIONS OF THE PARTIES

[5] The Board is being asked to address what is essentially a legal question.

[6] Heritage noted that the Board’s jurisdiction, as set out in s. 22(1) of the *Gas Distribution Act, 1997, c.4 (“Act”)*, is to “approve or fix just and reasonable rates, tolls or charges for the delivery of gas by a delivery system including related services”.

Heritage submitted that natural gas storage falls within the purview of related services and that the recovery of these costs should be regulated. Under the *Act* the transportation and delivery of natural gas is regulated but the commodity price is not. However, virtually all of the natural gas sold on the Heritage system is sold by Heritage as a marketer of gas. The continued build-out of Heritage's gas distribution system is, in part, dependent on competitively priced natural gas.

[7] Heritage advised that it has been in negotiations with Alton concerning a Tariff and Precedent Agreement. Alton is in the process of developing natural gas storage. In advance of signing an agreement Heritage requests Board approval to recover the cost associated with natural gas storage.

[8] If a favourable determination is made by the Board, Heritage advised it intends to submit a detailed application describing the costs of gas storage services and the methodology for recovery. Heritage outlined its natural gas storage requirements. Similar to other Canadian natural gas companies, Heritage's highest demand periods are in the winter and lowest demand periods are in the summer. Natural gas storage enables companies to purchase and store natural gas during the summer months, when natural gas prices are generally cheaper, in order to meet the increased demand in the winter months when natural gas is more expensive.

[9] Heritage advised that, to date, its source of supply has been offshore Nova Scotia. However, there continues to be a decline in production from the Sable Offshore Energy Project and there will be a future drop in production of the Deep Panuke Project over the lifespan of the project. Heritage stated:

Compounding its deliverability challenges is the fact that Heritage Gas' customers' winter gas needs often occur in heavily concentrated periods of several hours or days. During these peak periods, Heritage Gas' customers demand approximately five times the

volume of gas they need during lower-use, off-peak, periods in the summer. In order to meet its customers' needs during these peak swings in demand, Heritage Gas must have access to large volumes of natural gas that it can readily deliver to its customers through the distribution system.

Natural gas storage provides Heritage Gas with supply assurance in the face of declining production from the Sable Island supply basin, deals with deliverability requirements during peak heating season and addresses the desire to mitigate price spikes that occur in natural gas markets along the Eastern seaboard which will impact prices in Nova Scotia.

Natural gas storage will allow Heritage Gas to purchase natural gas during lower demand periods when gas prices may be low (i.e. summer), inject the natural gas into the storage facility, and then withdraw that natural gas during higher demand periods when gas prices may be high (i.e. winter). This will ensure that Heritage Gas has access to sufficient volumes of natural gas to meet its peak winter demand without resorting to the purchase of natural gas on the expensive "spot market".

[Exhibit H-1, p. 6]

[10] With its Application Heritage provided a report dated May 31, 2013, from ICF International entitled "Independent Assessment of Alton Natural Gas Storage" ("ICF Report").

[11] Although not strictly relevant to the legal question before the Board, the ICF Report does provide some important context. ICF advises that Heritage customers would benefit from the proposed storage, both in the short and long term. It advised that, based on the current forecast for gas prices, there would not be an identifiable period when storage costs exceed the savings realized from storage. ICF went on to state:

Based on our analysis, ICF concludes that for the Base Case natural gas market outlook, use of Alton Gas storage by Heritage Gas would significantly reduce the utility's expected supply portfolio cost, reducing costs to Heritage Gas consumers under all scenarios considered. This conclusion is robust across the full range of supply and storage scenarios considered. Based on our analysis, we would expect Heritage to see cost savings from the first year of storage service through the length of the storage contract. The basic conclusion that use of Alton storage capacity would reduce overall supply costs also holds even if Heritage Gas demand growth is slower or faster than projected, although the optimum amount of storage capacity would vary for alternative demand scenarios.

[Exhibit H-1, p. 9]

[12] The ICF Report notes that Heritage is at the end of a transmission system with limited supply sources of natural gas, making it difficult to source peak day supply

during North American peak periods. That has been obvious during the last two winters when natural gas prices have spiked substantially in Nova Scotia, in part due to pipeline constraints in the North Eastern United States. Storage can provide procurement flexibility when the gas is needed.

[13] Heritage noted:

- Natural gas storage will allow Heritage Gas to access supply basins with significant liquidity, in terms of greater production volumes and number of suppliers, such as the Western Canadian Supply Basin and the burgeoning Marcellus Basin. This will allow Heritage Gas to contract with a significantly greater number of suppliers and provide more flexibility to sell potential excess supply to more market participants when the Heritage Gas demand drops due to weather impacts or when unbundling is available to large users in Nova Scotia.

- ICF Analysis (p. 26 of ICF Report):

What effect would a natural gas storage facility have on future gas supply contracts? Storage should provide Heritage with additional flexibility in future contracting. Without storage, Heritage or any shipper with variable gas requirements would depend on a combination of base load and peaking (or swing) gas supply where the supplier would provide the flexibility. Such flexibility can be costly, since the supplier must manage supply and pipeline nominations in a way to allow swings in service. In addition, the price of gas in New England can experience dramatic intra-monthly volatility which also can contribute to higher costs. By nature, storage reduces these two key price expenses by providing peak supply purchased at more acceptable prices.

...

- Heritage Gas is located at the end of the M&NP-CA pipeline system and if there is a disruption, for any reason, gas supply for Heritage Gas' customers will likely be interrupted. Natural gas storage close to Heritage Gas' customer base would provide additional reliability to gas delivery to the Heritage Gas distribution system in the event of disruptions downstream of the M&NP-CA pipeline.

[Exhibit H-1, p. 11]

[14] With respect to the legal argument Heritage noted, and the Board agrees, that the *Act* does not directly address the circumstances of a local distribution utility using storage. The only reference to storage is found in s. 17 of the *Act* which states as follows:

17 Subject to such exemptions or conditions as prescribed, the holder of a franchise shall, without delay and with due care and diligence, receive, transport and deliver or store, without discrimination, all gas offered to its gas delivery system.

[15] Heritage argued that the *Act* contemplates a utility might store natural gas but does not provide any explicit direction in regard to the Board's jurisdiction. Heritage argued that storage is a related service under s. 22(1) of the *Act*:

However, Section 2(a) of the *Act* describes its purpose as follows:

*"2. The purpose of this Act is to
(a) provide a framework for the orderly development and operation of a gas delivery system in the Province; . . ."*

As part of that framework, the Board is provided with regulatory oversight of local distribution companies. In particular, the Board has the authority to approve the rates, tolls and charges for the delivery of natural gas.

Section 22(1) states:

*"22(1) The Board may, on its own initiative or on the application of a person having an interest, by order in writing, approve or fix just and reasonable rates, tolls or charges for the delivery of gas by a gas delivery system, **including related services.**" (emphasis added by Heritage)*

It is the view of Heritage Gas that the costs associated with the storage of natural gas falls within the jurisdiction of the Board to regulate the "related services" provided by the utility.

In a way, natural gas storage costs are no different from other operating costs incurred by Heritage Gas. Storage service is contracted and expenses are incurred to enable Heritage Gas to deliver natural gas to its customers in a safe and reliable manner. Generally, on a public policy basis, it is in the public interest for operating costs (including natural gas storage costs), to be subject to the overview and scrutiny of the Board. As noted previously, Heritage Gas is of the view that the scope of the Board's jurisdiction pursuant to the Gas Distribution Act is sufficiently broad to allow for this oversight.

[Exhibit H-1, p. 7]

[16] The Minister of Energy supported Heritage's Application. The Minister noted as follows:

The Department believes that best value is ensured with regulatory oversight of costs and how they are recovered from customers. In this case the Department agrees with Heritage that natural gas storage falls within the Nova Scotia Utility and Review Board's purview of "related services" and should be regulated.

[Exhibit H-5, p. 2]

[17] PHP also supported Heritage's Application noting that a favourable decision would provide Heritage with additional certainty on cost recovery to support the

potential construction and commissioning of a storage facility. PHP stated that storage would have benefits not only for Heritage's customers, but benefit for electrical customers in Nova Scotia because NSPI uses natural gas.

[18] The CA took the position that the Application is premature and asked the Board to direct Heritage to complete its negotiations with Alton and reapply to the Board so that a review of jurisdictional issues can be undertaken in the context of a specific proposal.

[19] The CA noted that in other jurisdictions gas storage facilities have been viewed as ancillary to gas supply or gas distribution or both.

III ANALYSIS AND FINDINGS

[20] The Board believes it has a sufficient factual basis to make a decision in this matter without a signed Tariff and Precedent Agreement with Alton. The prudence of any potential agreement is for a subsequent proceeding.

[21] Based on the ICF Report, it appears storage has the potential to provide significant benefits, in terms of cost savings, to Heritage's customers and help prevent the severe volatility in gas prices they have experienced for the past two winters. The potential dollar savings outlined in the ICF Report, while filed confidentially, are material.

[22] The *Interpretation Act*, R.S.N.S., 1989, c. 235, Section 9(5) provides guidance with respect to the interpretation of statutes:

Interpretation of words and generally

9 (5) Every enactment shall be deemed remedial and interpreted to insure the attainment of its objects by considering among other matters

- (a) the occasion and necessity for the enactment;
- (b) the circumstances existing at the time it was passed;
- (c) the mischief to be remedied;

- (d) the object to be attained;
- (e) the former law, including other enactments upon the same or similar subjects;
- (f) the consequences of a particular interpretation; and
- (g) the history of legislation on the subject.

[23] The purpose of the *Act* is to provide a framework for the orderly development and operation of a gas delivery system in the province. As noted by Heritage, s.17 of the *Act* contemplates that the franchisee will store gas. That section reads as follows:

17 Subject to such exemptions or conditions as prescribed, the holder of a franchise shall, without delay and with due care and diligence, receive, transport and deliver or store, without discrimination, all gas offered to its gas delivery system. [Emphasis added]

[24] The Board's powers are found in s. 22(1):

22(1) The Board may, on its own initiative or on the application of a person having an interest, by order in writing, approve or fix just and reasonable rates, tolls or charges for the delivery of gas by a gas delivery system, including related services. [Emphasis added]

[25] Read together those two sections, and the factual basis provided by Heritage, suggest to the Board that storage is a "related service". The Board does note the comments of the Minister that as a matter of public policy "best value is ensured" with the regulatory oversight of storage costs. The Board agrees that the scope of the Board's jurisdiction, pursuant to the *Act*, is sufficiently broad to allow for this oversight.

[26] No other provisions of the *Act*, including the definition of gas delivery system, appear to the Board to assist in answering this question.

[27] Accordingly, the Board finds that the prudently incurred costs of natural gas storage may be included with Heritage's cost of service.

[28] The Board emphasizes that the prudence of any arrangement entered into by Heritage can and will be tested in a future proceeding.

[29] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 20th day of February, 2014.

Peter W. Gurnham