



EB-2005-0449

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

AND IN THE MATTER OF an Application by Union Gas
Limited, pursuant to section 36(1) of the *Ontario Energy
Board Act*, 1998, for an order or orders approving or
fixing just and reasonable rates and other charges for the
sale, distribution, transmission, and storage of gas as of
January 1, 2006;

BEFORE: Paul Sommerville
Presiding Member

Cynthia Chaplin
Member

Cathy Spoel
Member

DECISION ON MOTION

October 13, 2005

Union Gas Limited (“Union”) filed an application (the “Application”) dated July 29, 2005 with the Ontario Energy Board (the “Board”) for an order or orders approving or fixing just and reasonable rates and other charges for the sale, distribution, transmission, and storage of gas commencing January 1, 2006. The Board assigned file number EB-2005-0449 to the Application.

In particular, the Application sought Orders from the Board permitting Union to: (1) increase existing rates by 5.4%, commencing in 2006, and (2) continue the earnings sharing mechanism, currently in place for 2005, into 2006.

On August 26, 2005, the Board issued a Notice of Application which included directions on how to participate and which was published throughout Union’s service territory. As part of the Notice, the Board set September 20 and September 21, 2005 as the dates to hear several procedural matters. Participants were asked to be prepared to answer the following questions:

1. Does the material filed by Union Gas form a sufficient evidentiary base from which to evaluate the company’s revenue requirement for 2006?
2. If not, what alternative approaches could be used to determine an appropriate rate adjustment, if any, for 2006? The Board is seeking comment on potential options for indexing existing rates for 2006.

In a written submission dated September 15, 2005, Union addressed the Board’s two questions and proposed that an index-based approach could be used for rate setting for the 2006 calendar year. This proposal effectively replaced Union’s original Application for a 5.4% increase with an alternative proposal that carried a lower percentage increase while still including the continuation of the current earnings sharing mechanism.

On September 20, 2005, upon canvassing the parties present at the hearing, the Board convened a settlement conference for the balance of the day to assess the prospects

for a settlement of the issues amongst the parties. On September 21, 2005, the Board was informed that no settlement could be reached. Consequently, the Board proceeded to hear submissions from the parties on the two questions.

At the hearing, Union informed the Board that it intended to amend its Application and that it would file supplementary evidence to provide for its alternative index-based rate setting approach. To this end, Union filed an amended application, together with supplementary information, on September 23, 2005. The amended application requested that as an alternative to the original 5.4% increase, an index-based adjustment mechanism of 2%, based on Ontario CPI, be used to set 2006 rates and that a further allowance of 0.6% be added for Union's Workforce Development and Enhancement Initiative (WDEI) for a total increase of 2.6%.

BOARD FINDINGS

With respect to the first question posed in the Board's Notice, the Board concurs with the parties and finds that the evidence filed to date does not represent a sufficient evidentiary basis to proceed with a cost of service approach to rate setting for 2006. The Board also notes Union's statement that the information for a traditional cost of service review does not exist and therefore cannot be provided in the time frame required for rates to be approved by January 1, 2006.

The Board must therefore decide whether an alternative approach to rate setting, if any, is warranted. Union has proposed a formulaic approach using the Consumer Price Index ("CPI"), with an additional adjustment to account for costs related to its aging workforce. Union submitted that timing pressures and the prima facie evidence of increased costs provide sufficient grounds for the Board to consider such an approach. Other parties challenged Union's approach and some proposed other index-based approaches, including Union's prior approved PBR adjustment mechanism.

While the Board has traditionally used a cost of service approach to rate setting, the OEB Act does not require the Board to take this or any other specific approach to

determine whether rates are just and reasonable rates. However, any approach taken by the Board requires a sufficient evidentiary basis for the Board to make an informed decision in the particular circumstances of each case that the rates set by the Board are just and reasonable.

The Board has used an index-based adjustment process to approve rates in two circumstances: to allow Enbridge to have its rates approved in a timely fashion following several years of retroactive approvals, and as part of a broader PBR process. In the Board's view, neither circumstance applies to Union's current situation. Obviously, an adjustment is not being considered within the context of a broader PBR or incentive regulation process, and therefore the latter approach is not relevant. The circumstances around the Enbridge approach require further consideration.

There were two specific circumstances surrounding the Enbridge approach that are relevant. First, the adjustment mechanism for Enbridge was designed to address a particular set of extraordinary circumstances, namely to bring Enbridge "back on track" to an appropriate regulatory schedule. Second, the index-based adjustment was applied to rates which had quite recently been subject to a thorough cost of service review.

Neither circumstance applies to Union in this case. The fact that Union plans to file its full cost of service evidence for 2007 rates in December of this year makes the position even more difficult. Once this evidence is filed, the rationale for an indexing approach weakens considerably.

The Board understands the pressures imposed by the regulatory agenda; however, it is up to Union to resource itself appropriately so that it may achieve its priorities. It is inappropriate to seek to abbreviate the proceeding or justify an index-based approach solely on the basis of timing concerns. Further, Union seeks to apply the adjustment to 2005 rates, which are, in turn, adjusted 2004 rates. A substantial period of time has elapsed since a cost of service review has been conducted. This raises a number of substantive issues about the appropriate base for any index-based adjustment, which

requires additional evidence beyond that which Union has provided to date. General evidence of cost pressures and a possible revenue deficiency in a future year are not sufficient grounds on their own to support a formulaic adjustment approach, particularly given that the evidence filed to date indicates a revenue sufficiency for 2005.

It is noteworthy that since Union's last cost of service application, which was heard in late 2003 for 2004 rates, the Company has earned substantially more than the regulated rate of return.

If Union wishes to pursue this application it would be necessary, at a minimum, for it to provide evidence addressing the following:

- Adjustments to the 2005 rates to set the base for any formulaic adjustment (including consideration of long term debt rates, return on equity, and excess earnings levels in 2005)
- Alternative formulas/indices (including GDPPI, productivity factors, input price adjustments)
- Adjustments for particular factors (including WDEI and the recent merger between Duke and Cynergy)
- Structure of the earnings sharing mechanism
- Application of the adjustment (including whether the adjustment is before or after the Delivery Commitment Credit (DCC) adjustment, and whether the adjustment should be applied to the fixed and/or variable portions of the rate)

In providing guidance to the Parties, the Board is motivated by pragmatic considerations as well as issues of regulatory principle. As a matter of regulatory principle, the Board concludes that the amended application, as it stands, does not meet a reasonable standard of completeness. With respect to more pragmatic considerations, the Board notes Union's explicit desire to preserve the timing of both the Natural Gas Forum processes and its own 2007 rates case. While the 2006 process might be expedited to some extent, the Board concludes that setting new rates for January 1, 2006 is not achievable, given the evidentiary requirements and the timing criteria established by

Union. The Board further notes that adjusting rates on a retroactive basis can be problematic, and raises separate issues.

The Board understands the concerns expressed by parties on DSM and fuel switching issues. Intervenors submitted that the Board should direct Union to file its 2006 DSM plan and related materials by October 31, 2005, and to order that fuel switching issues be addressed in the DSM process. Given Union's stated commitment to meet the specified date and to accept fuel switching issues as part of that process, the Board finds that no order is required. Further, given that the DSM process is a separate process in any event, the Board will not order Union to prepare evidence related to the questions raised by Pollution Probe. However, the Board notes that, as discussed above, if Union wants to expedite the process, it would do well to consider the requests of Pollution Probe and address them on a proactive basis.

If Union decides not to proceed with its application as amended, it must still prepare a rate order for 2006 which should include the further implementation of the DCC reduction and a continuation of the earnings sharing mechanism.

The Board will determine awards of costs associated with this Decision as part of an overall determination of costs for the Application. Eligible intervenors shall submit any costs claims as soon as possible.

DATED at Toronto, October 13, 2005.

ONTARIO ENERGY BOARD

Signed on behalf of the Panel

Original Signed By

Paul Sommerville
Presiding Member