Ontario Energy Board

Commission de l'Énergie de l'Ontario

EB-2011-0210

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

AND IN THE MATTER OF an Application by Union Gas Limited 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, 2013.

BEFORE: Marika Hare
Presiding Member

Karen Taylor
Board Member

DECISION AND ORDER

Union Gas Limited ("Union") filed an application on November 10, 2011 with the Ontario Energy Board (the "Board") under section 36 of the *Ontario Energy Board Act, 1998* for an order of the Board approving or fixing rates for the distribution, transmission and storage of natural gas, effective January 1, 2013 (the "Application"). The Board assigned file number EB-2011-0210 to the Application and issued a Notice of Application on December 1, 2011. This is the first cost-of-service application for setting rates since 2007. From 2008 to 2012 rates were set under an Incentive Regulation Mechanism ("IRM") which adjusted rates through a mechanistic formula.

The Board issued its Procedural Order No. 1 on January 11, 2012, which established the approved list of intervenors for this proceeding. The list included:

- Association of Power Producers of Ontario (“APPrO”)
- Building Owners and Managers Association Toronto (“BOMA”)
- Canadian Manufacturers and Exporters (“CME”)
- City of Kitchener (“Kitchener”)
- Consumers Council of Canada (“CCC”)
- Enbridge Gas Distribution Inc. (“Enbridge”)
- Energy Probe Research Foundation (“Energy Probe”)
- Federation of Rental-housing Providers of Ontario (“FRPO”)
- Industrial Gas Users Association (“IGUA”)
- Jason F. Stacey
- Just Energy Ontario LP (“Just Energy”)
- London Property Management Association (“LPMA”)
- Ontario Association of Physical Plant Administrators (“OAPPA”)
- Ontario Power Generation (“OPG”)
- School Energy Coalition (“SEC”)
- Six Nations Natural Gas Company Limited (“SNNG”)
- Shell Energy North America (Canada) Inc. (“Shell Energy”)
- TransAlta Generation Partnership (“TransAlta Generation”)
- TransAlta Cogeneration LP (“TransAlta Cogeneration”)
- TransCanada Pipelines Limited (“TCPL”)
- TransCanada Energy Limited (“TCE”)
- Vulnerable Energy Consumers Coalition (“VECC”).

The Board also determined that APPrO, BOMA, CME, CCC, Energy Probe, FRPO, IGUA, LPMA, OAPPA, SEC, and VECC are eligible to apply for an award of costs under the Board’s *Practice Direction on Cost Awards*.

Union filed its Application on the basis of US Generally Accepted Accounting Principles (“USGAAP”). At the same time, Union sought approval to move to USGAAP from Canadian GAAP as part of this Application. The Board decided to first deal with Union’s request for the adoption of USGAAP for regulatory purposes (the “Preliminary Issue”) prior to processing the Application in accordance with the Addendum to Report of the Board: Implementing International Financial Reporting Standards in an Incentive Rate Mechanism Environment (the “Addendum Report”).

In Procedural Order No. 1 the Board established a timeline for interrogatories, interrogatory responses, submissions, and reply submissions related to the Preliminary Issue in advance of further procedural steps. In addition, the Board adopted the

evidence related to the USGAAP issue from Union's 2012 IRM Proceeding EB-2011-0025 (the "Adopted Evidence").

Submissions were received from the LPMA, CCC, SEC, CME, APPrO and Board staff. LPMA, CCC, SEC and Board staff supported the request by Union for the adoption of USGAAP for regulatory purposes. CME and APPrO were also supportive of Union's request but provided some proposed conditions of approval.

The Board issued its Decision on the Preliminary Issue and Procedural Order No. 2 on March 1, 2012. The Board granted Union approval to use USGAAP for regulatory purposes. The Board also set out the timelines for the Issues Conference, Issues Day Hearing, filing of interrogatories and responses to interrogatories by Union in this Procedural Order.

Procedural Orders No. 3 and No. 4 set timelines for the next procedural steps, including setting dates for the Technical Conference and the Settlement Conference.

The Board revised some of the timelines for interrogatories and filing intervenor evidence in Procedural Order No. 5 after considering a letter filed by TCPL that requested revised dates to accommodate timelines related to the hearing of its application before the National Energy Board.

TCPL filed a Notice of Motion on May 17, 2012. The Motion requested the following:

1) An Order requiring Union to provide proper answers to the Interrogatories identified in Appendix "A" to the Notice of Motion, or such other information as the Board considers appropriate.

2) An Order requiring Union to file with the Board unredacted copies of pages in Interrogatory Responses that were filed in redacted form as part of Union's Interrogatory Responses to TCPL, so that the Board could assess the reasonableness of the claims for confidentiality and make such order as it considers appropriate in that regard.

The Board in Procedural Order No. 6, issued on May 18, 2012, decided that it would not hear the second request as part of the TCPL Motion as there were other exhibits, not

mentioned in TCPL's Motion, which were filed under confidential cover. The Board in Procedural Order No. 6 established a separate process for reviewing Union's claims for confidentiality.

The Board heard the Motion filed by TCPL by way of written hearing. Procedural Order No. 6 made provision for all parties to the proceeding to file submissions on the merits of TCPL's motion and for TCPL to file reply submissions. This process was completed on June 8, 2012.

TCPL, BOMA and Union filed submissions on TCPL's motion. The interrogatory information sought by TCPL related primarily to Union's Parkway West project which purports to provide for loss of critical unit protection at Parkway.

With respect to the Parkway West project questions, TCPL's position was that the information that it was seeking was necessary for the Board to evaluate the reasonableness of Union's proposed capital expenditures. Union submitted that the information requested by TCPL was not relevant to Union's Application as the Parkway West project would not come into rate base until 2014 and did not impact 2013 rates. Union's position was that providing such further information could have no bearing on deciding the issues before the Board in this Application.

BOMA's submissions largely supported TCPL's request for Union to provide answers to the TCPL Parkway West interrogatories.

The Board in its Decision dated June 15, 2012, granted the Motion and required Union to provide responses to the interrogatories.

With respect to the relevance of the Parkway West interrogatories, the Board indicated that a review of the forecast capital spending plan was a conventional aspect of a cost of service rebasing process. The Board recognized that the specific projects that were the focus of the interrogatories at issue were not expected to close to rate base within the test year, and that the Board was not conducting a review of the projects for approval. However, the Board has commonly reviewed capital spending forecasts as part of a cost of service review, and determined that it would do so in this case.

The Board noted that the proposed projects may have important implications for Union's operations during the following year, in particular if Union is again entering into an incentive regulation regime for rate-setting. The Board indicated that it would be remiss in considering this cost-of-service application if it did not ensure that it had as clear a picture as possible of the significant developments likely to arise within the next regulatory rate-setting period.

On the issue of confidentiality, the Board determined that, except for the benchmarking studies, the information that Union proposed to redact was not confidential, and that the full and unredacted versions should form part of the public record. With respect to the benchmarking studies, the Board agreed with Union that the specific rankings of the studies' participants (other than Union) should not be on the public record, and therefore allowed the redactions. However, the Board required that the list of the participants to the studies be made public where it was included in the study. The Board noted that in assessing the relevance of a benchmarking study, it was important that the "comparators" be known.

As per Procedural Order No. 4, a Settlement Conference was held from June 6 to June 18, 2012 between Union and intervenors to settle some or all issues. In broad terms, the parties reached an agreement with respect to rate base and cost of service for the test year, being the issues under headings Exhibit B – Rate Base and Exhibit D – Cost of Service, respectively, with the exception of matters pertaining to Gas Supply Planning (Issue 3.14) and capital expenditures relating to Parkway West (Issue 1.1). The parties also reached agreement on several other issues, each of which were separately identified as settled in the Settlement Agreement. As a result of the Settlement Agreement, the updated revenue deficiency proposed by Union was reduced to $54.524 million from $71.4 million. The Board considered and accepted the Settlement Agreement as reasonable.

The Board addresses below the issues that remained unresolved.

UNSETTLED ISSUES

The following issues were considered by the Board:

- Weather Methodology
- Normalized Average Consumption ("NAC")

- Operating Revenue
- Other Revenues
- Ex-franchise Revenue
- Optimization and Gas Supply Plan
- Cost of Capital
- Cost Allocation
- Rate Design
- Deferral and Variance Accounts
- Parkway West
- Other Issues

WEATHER METHODOLOGY

Union has proposed to use a 20-year declining trend to derive the total Heating Degree Days ("HDD") estimates for 2012 and 2013. The 2013 weather normal forecast is based on the 20-year declining trend weather normal methodology. In RP-2003-0063, the Board approved a 70:30 weighting of the 30-year average forecast and the 20-year declining trend. The Board directed Union to change the weighting by 5% annually, until the methodology reached a 50:50 weighting. However, based on the Settlement Agreement approved by the Board in EB-2005-0520, Union's current methodology in rates reflects a 55:45 weighting of the 30-year average and the 20-year declining trend methodology. The 50:50 weighting approved by the Board was not achieved as a result of that Settlement Agreement.

Intervenors and Board staff argued that Union had not adequately justified the use of a 20-year declining trend. They submitted that Union had not presented other methodologies to demonstrate that the 20-year declining trend is superior to other methodologies. LPMA submitted that Union had merely compared the proposed 20-year declining trend with the current approach approved in rates. LPMA further submitted that Enbridge in the EB-2006-0034 proceeding had presented an exhaustive analysis of 9 different forecasting methodologies that were ranked based on a number of statistical measures over a number of different periods[1], and that Union did not do such an extensive analysis in this case. Board staff submitted that Union had not provided sufficient evidence for the Board to make an informed decision. Board staff further

[1]Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p.31.

argued that the Board had no basis for determining if the 20-year declining trend is the most appropriate and accurate forecasting methodology for Union.

Similarly, VECC submitted that Union presented more models in the 2004 proceeding (RP-2003-0063) where it presented six different methodologies in addition to the 20-year declining trend.

In its reply submission, Union submitted that intervenors had several opportunities to test other models and they could have asked Union for additional evidence during the discovery process, but did not do so. Union submitted that the Board should not reject the 20-year declining trend on the basis that there is some other methodology which may provide better results. Union submitted that the Board should make a decision on the basis of what is filed in evidence and that is a choice between the 20-year declining trend, the existing method and the 30-year average.

LPMA submitted that Union only considered a trend methodology based on a 20-year time horizon with no other explanatory variables other than the trend used to explain the fluctuation in heating degree days. Further, Union did not consider adding any other variables to the trend model to see if it could find a better equation that might improve the forecast.[2]

Some intervenors (LPMA, VECC and Energy Probe) specifically argued that there is a significant flaw in the equations used to forecast degree days for the Test Year. They submitted that the equations are not statistically significant even at an 85% level of confidence. In reply, Union submitted that the 20-year declining trend was statistically superior to the blended and the 30-year average methodology. While the results of the 30-year average are significant at the 30-45% confidence level, the existing methodology is significant at the 70% confidence level. Union submitted that intervenors were critical of the 20-year declining trend but were overlooking the weakness and bias that exist in the existing methodology and the 30-year average.

Energy Probe also submitted that Union had not investigated zone based Heating Degree Days forecast methodologies as was done by Enbridge. Board staff made a similar submission that Union should have considered the possibility of different

[2] Oral Hearing Transcripts, EB-2011-0210, Volume1 at pp. 44-46.

forecasting approaches across the different regions. Energy Probe submitted that Union was using Pearson Airport Data for weather which was not a fair representation of Union's franchise area. In reply, Union submitted that there was no evidence to support Energy Probe's position and the evidence indicates that the weather in Union's franchise area in the North and the South is highly correlated to Pearson, at a correlation of over 90%.

Board staff and VECC further submitted that Union had not performed some of the tests that would validate its regression model. This includes testing for heteroskedasticity.[3] The presence of heteroskedasticity can invalidate statistical tests of significance that assume that the modelling errors are uncorrelated and normally distributed and that their variances do not vary with the effects being modelled. VECC submitted that testing for heteroskedasticity was not a major exercise and therefore should have been undertaken.

SEC and Board staff submitted that the 20-year trend possibly results in a steep downward sloping curve even though it may be slicing the middle of the data denoting better symmetry. Board staff noted that this results in far lower Normalized Average Consumption numbers for 2012 and 2013. SEC noted that the 20 years is the period of trend that produces the steepest downward sloping curve. In reply, Union submitted that Board staff was focusing on the volatility of NAC which was an indirect argument since weather is one of the components in the NAC calculation.

Many intervenors and Board staff submitted that based on the evidence, the Board should approve a 50:50 blend of the 30-year average and the 20-year declining trend for 2013. BOMA, however, recommended that the Board should approve the current approach in rates which is the 55:45 blend.

LPMA submitted that the 20-year trend component of the blended methodology should not be Union's 20-year declining trend forecast as included in the evidence. First, the 20-year trend forecast as filed by Union should be updated to reflect actual 2011data, as should the 30-year moving average. Second, the 20-year declining trend equations modified for a structural shift that is shown in Attachments 1 of 3 of Exhibit J1.3 should be used in place of the equations shown in Attachments 2 and 4.

[3]Heteroskedasticity occurs when the standard deviations of a variable monitored over a specific amount of time, are not constant.

LPMA submitted that for the Southern service area the equation that includes the structural shift variable with an overall fit confidence interval of more than 99% should be used. The test year forecast from this equation from a statistical point of view is 3,816 HDD which should be used in the weighting for the 2013 forecast.

In the North, LPMA submitted that the two equations were both a good fit with an overall confidence level of more than 99%. However, the equation with the structural shift variable explains a higher proportion (56%) of the variability in the data as compared to the equation without it. The test year forecast from the better fitting equation from a statistical point of view is 4,844 HDD. LPMA submitted that this should be used in the weighting for the 2013 forecast.

Lastly, Board staff and LPMA requested the Board to direct Union to present better evidence at the next cost of service proceeding. LPMA submitted that the Board should direct Union to conduct a comprehensive review of at least the same forecasting methodologies as reviewed by Enbridge in both their EB-2006-0034 and the current EB-2011-0354 rates proceedings and provide that analysis at the next rebasing proceeding.

In reply, Union submitted that the introduction of a dummy variable in 1998 by LPMA is highly subjective. Union indicated that by introducing a dummy variable, LPMA was suggesting that the weather had changed in 1998 and became colder going forward. Union submitted that this was subjective and introducing a dummy variable could lead to arguments in future proceedings with respect to when a dummy variable should be introduced. Union submitted that the 20-year declining trend ranks above the LPMA dummy variable methodology, considering that the dummy variable methodology shows large mean percent and root mean square errors.

Union submitted that the Board should focus on the evidence presented and the evidence shows that the 20-year declining trend is superior to the existing and the 30-year average methodologies. Consequently, the Board should approve Union's proposal.

Board Findings

In the RP-2003-0063 proceeding, Union sought to use a 20-year declining trend methodology. In that Decision, the Board approved an initial 70:30 weighting of the 30-year average forecast and the 20-year declining trend. The Board directed Union to change the weighting by 5% annually, until the methodology reached a 50:50 weighting.

In this proceeding, intervenors and Board staff have submitted that Union failed to bring forward or discuss other methodologies. Union, in its reply argument, submitted that intervenors did not raise concerns or provide additional evidence during the discovery process. The Board believes that it is the responsibility of the applicant to provide the evidentiary basis to support its position. Union failed to review other scenarios and provide the Board with the information and statistical support necessary for the Board to determine that the 20-year declining trend is the most appropriate methodology. Even the 50:50 blended methodology that was approved in RP-2003-0063 was not discussed by Union in its Application, but was only reviewed through interrogatories and evidence that emerged during the proceeding.

Union submitted that Board staff erred when it focussed on the volatility of NAC while discussing weather. However, the Board considers that it is clear that the weather is becoming more volatile, and that it is desirable to adopt a methodology that smooths this volatility. In the RP-2003-0063 Decision, the Board noted that both the 30-year average and the 20-year declining trend have advantages. The 20-year trend may track through the middle of the data as Union claims and would respond more quickly to changes in short-term trends but would also be more volatile. On the other hand, the 30-year average will respond more slowly to changes but would be less volatile.[4] During this proceeding Union has agreed that the weather is becoming more volatile.

Union, in reply argument, stated on page 85:

> And the evidence is, while it may be getting warmer as a trend, weather is still – and getting more so – volatile and that the experience in the weather charts we looked at shows that there are wide swings in the weather year to year, and frankly, within a year.

[4]Decision with Reasons, RP-2003-0063, March 18, 2004 at p. 22.

The Board finds that since the 20-year declining trend reflects a shorter time period, it would be more likely to be affected by large variations in weather between one year and another. In other words, it would not perform as well as the blended methodology to smooth the effects of a particular year that is warmer or colder. The Board believes that use of the 20-year declining trend methodology could expose ratepayers to wider variations in costs from year to year since the methodology may not produce stable results and is susceptible to volatile weather patterns.

The Board directs that a 50:50 blended approach of the 20-year declining trend and the 30-year average methodology be adopted. Union is further directed to make the required adjustments to incorporate 2011 actual data, thus using the most recent and available data.

The Board does not agree with LPMA that a dummy variable should be introduced. The Board believes that this is a subjective adjustment to the methodology. The Board finds that a dummy variable is not necessarily required to account for the upward move between 1998 and 2000.

The Board directs Union to reflect the appropriate adjustments in the Draft Rate Order.

Union has submitted that its weather data for its Northern and Southern franchise areas is highly correlated. The Board does not agree that a high level of correlation necessarily implies that it is appropriate to use the same forecasting methodology in each of the North and South franchise areas. Union should consider analyzing each of the weather stations it utilizes to arrive at a weighting of its Southern and Northern degree days. A uniform approach may not be suitable for Union's service areas that exhibit wide weather variations between the North and South.

The Board does not see the need to provide direction to Union with respect to future filings in the event that Union chooses again to apply to change the degree day methodology. As stated earlier in this Decision, it is the applicant's responsibility to present sufficient evidence to demonstrate why a change in methodology or approach is appropriate.

NORMALIZED AVERAGE CONSUMPTION ("NAC")

Union's forecast estimates of NAC are prepared for the residential customers by individual rate class. Commercial NAC estimates are first prepared for the total commercial service class, then converted to regional estimates and finally allocated to the individual rate classes on the basis of historical volumetric shares. The industrial market demand is determined by a total volume equation and average consumption estimates are then subsequently derived. The NAC forecast for residential and commercial customers incorporates assumptions related to several demand variables: weather normal, energy efficiency, total bill amounts, fall seasonal weather and structural trend variables.

Residential NAC estimates are prepared separately for Union South and North customers. The residential econometric forecasting follows the methodology used in EB-2005-0520. The NAC estimates are the product of two regression equations: an average use per customer equation and a total volume equation. The average of the two econometric demand estimates is then adjusted for the forecast demand side management program NAC impact. The commercial NAC forecast estimates are obtained from regression analysis of commercial consumption data from all general service rate classes.

Intervenors and Board staff submitted that the NAC forecast for the residential and commercial markets are significantly lower than the historic trend. Board staff submitted that Union has forecasted a decline of 5.1% from 2011 to 2013 in the M2 residential market, which is significantly higher than an average annual reduction of approximately 1.5% from 1992 to 2011. LPMA submitted that Union was forecasting that the percentage decline in non-weather related average residential use will double in the bridge and test years.

Similarly, with respect to Rate 01, LPMA submitted that the residential average annual use fell by 0.2% in 2006 to 2011, 1.3% in 2001 to 2011, and 1.4% in 1991 to 2011. However, for the bridge and test years, Union has forecasted a decline of 2.4% per year for the bridge and test years reflecting an increase in the rate of decline by one full percentage point compared to historical rates. LPMA and VECC submitted that Union has not provided any evidence to support this accelerated decline in average use. LPMA noted that the rate of decline due to furnace efficiency improvements has not

accelerated, and neither has the reduction due to Demand Side Management ("DSM") initiatives.

LPMA, VECC, CCC and Energy Probe submitted that the Board should approve a forecast for the two residential classes that reflects a decline in average use in the bridge and test years that is consistent with the historical data. CCC and LPMA submitted that a reduction of 1.4% per year for both classes is reasonable and consistent with the long term trend. This would reduce the M2 average use from 2,264 m^3 in 2011 to 2,201m^3 in 2013 and the 01 average use from 2,269 m^3 to 2,206m^3 over the same period. VECC submitted that the NAC forecast for M1 and Rate 01 should be increased by 1.1% for 2012 and 2013. Energy Probe further submitted that the Board should continue the Average Use True Up Variance Account (the "Average Use Account", No. 179-118) in 2013.

LPMA and Board staff expressed similar concerns with respect to the decrease in average use forecast for the old rate M2 and Rate 01. While the annual percentage decline between 1991 and 2011 is only 0.4%, Union has forecasted a reduction in commercial old rate M2 by 3.4% on an annualized basis for 2011 to 2013. LPMA submitted that over the last 5 and 10 year periods, the average use for these customers had actually increased. Union supported the forecasted decrease by stating that the increase in average use in this category in 2011 was an outlier.

LPMA further submitted that the commercial use per customer equation used by Union did not include any explanatory variables related to the economy or the relative price of natural gas versus other energy sources, such as electricity. LPMA submitted that the increase in 2011 could be explained by the fact that the economy in 2011 was back to near pre-recession levels and natural gas prices have been at record lows while electricity prices have continued to rise.

With respect to commercial Rate 10 volumes, LPMA submitted that the forecasted decline of 1.7% per year is not reasonable considering that the average use in this category is higher in 2011 than it was in any previous year. Moreover, the general trend has been higher over the last decade. LPMA submitted that the Board should approve a forecast for the three commercial classes that reflects a decline in average use in the bridge and test years that is consistent with the historical data. LPMA submitted that a

reduction of 0.4% per year for commercial M2, and 1.0% for commercial 01 is reasonable and consistent with the long term trend.

None of the intervenors made a submission on the industrial average use forecasts. LPMA submitted that the forecasted average uses for the Rate 10 and M2 category were plausible.

In reply, Union submitted that the NAC calculations for the various residential, commercial and industrial components of the general service market are checked for specification every year and where appropriate have been re-specified. Union further noted that the results are statistically significant at the 95% level of confidence.

Union submitted that the intervenors had not challenged the statistical validity of the results of the NAC methodology but rather argued that the results could not be correct. Union submitted that the Board should reject the arguments forwarded by intervenors and approve the NAC forecast methodology as it has done in the past.

Union further submitted that should the Board have any concerns with respect to the NAC forecast, it could continue maintaining the Average Use Account that was in place during the incentive regulation period. Although Union did not prefer this approach, it indicated that continuing the deferral account would resolve the dispute around the NAC forecast. Under that option, Union submitted that the Board could include Union's NAC forecast in rates and apply the Average Use Account to track any changes.

Board Findings

The Board notes that Union's proposed NAC calculations forecast a much larger decrease than historic rates of decline. However, the Board believes that an arbitrary increase in the NAC numbers is not appropriate, given that Union's NAC numbers have been derived using econometric models that were previously approved by the Board. Moreover, moving to the 50:50 blended weather methodology will likely result in changes to Union's NAC calculations.

The Board therefore accepts the NAC forecast in rates as proposed (subject to an update for the approved weather methodology) by Union but finds that the continued operation and use of the Average Use Account for the 2013 test year is appropriate and

is fair to both Union and ratepayers. The Board directs Union to revise the NAC calculations based on the Board approved weather methodology and is directed to incorporate the revised numbers in the Draft Rate Order.

OPERATING REVENUE

Customer Attachments

Union has forecasted modest increases in customer attachments over the 2011 to 2013 period. In its Application, Union forecasted customer attachments of 19,510, 20,380 and 22,491 in 2011, 2012 and 2013 respectively.

Board staff submitted that Union had not included customer attachments related to the Red Lake project. At the hearing, Union confirmed that it expected to add approximately 800 customers in the community of Red Lake by 2013. Board staff submitted that although Union included the costs of the project in rate base, the revenues had not been accounted for in the current Application. Board staff submitted that as a matter of principle Union should include conversions related to Red Lake in its Application including the distribution revenues that are attributed to these attachments.

LPMA submitted that Union had under forecasted customer attachments in three of the past four years. The average under forecast number in 2008, 2010 and 2011 was 6,455, while in 2009, when the impact of the recession hit the housing market, Union over forecasted by 2,354 additions.[5] LPMA submitted that the average variance over the four years was 4,253. LPMA therefore submitted that the Board should increase the general service customer forecast by 4,250 in both the bridge and test years.

In reply, Union submitted that year-to-date, it was tracking lower than its forecast of total billed customers. The actual total number of billed customers as of June 2012 was 1,366,306 which represented a deficit of 399 customers as compared to the forecast.[6] Union therefore submitted that there was no reason to increase Union's customer attachment forecast for 2012 or 2013. With respect to the addition of Red Lake customers, Union submitted that revenues attributed to Red Lake were not material and this would not reach the materiality threshold as defined by the Board.

[5]Exhibit J.C-1-1-5.
[6] Oral Hearing Transcripts, EB-2011-0210, Volume 1 at p. 59.

Board Findings

The evidence indicates that Union is tracking marginally behind its total customer billed forecast for 2012. The Board sees no reason for increasing the forecast by 4,250 customers. Although LPMA refers to previous under forecasted numbers in 2008, 2010 and 2011, there is no evidence that such a trend will necessarily be continued. The Board finds that Union's forecast is reasonable, with one exception as noted below.

The Board believes that the 800 customers that Union has forecasted to attach in Red Lake must be included. Although this increase may be immaterial, it is based on an undisputed planning input. Union has included the capital costs of this project in rate base and the Board sees no reason for not including the revenues from these additions in the 2013 operating revenues. Accordingly, the Board directs Union to increase the customer forecast by 800 customers for 2013.

Contract Customer Demand Forecast

Union segments the contract customer market into different sectors. They include gas fired power generation, steel, refinery and petrochemical, greenhouse, wholesale and broad-based commercial and industrials ("LCI/Key"). The volume and revenue forecasts for contract customers are developed using two methodologies. An econometric forecast is developed for the majority of the customers and a detailed bottom-up forecast is developed for the large T1 and Rate 100 customers.

For the small to mid-size contract markets represented by the LCI and Greenhouse market sectors, Union uses econometric analysis to forecast consumption requirements. For the remainder of the contract market, Union uses a bottom-up approach given its extensive understanding of these accounts through ongoing interactions between the customer and the account manager.

APPrO in its submission proposed an overall increase of $3.09 million to the revenue forecast with respect to the contract market. This includes a power revenue commodity increase of $1.0 million, incremental fuel associated with the commodity revenue of $0.14 million, a T1 billing contract demand overrun revenue of $0.75 million and other contract overrun revenue of $1.2 million.

APPrO in its submission noted that, in accordance with provincial policy, coal-fired generation is in the process of being phased out. APPrO submitted that gas-fired generation has replaced much of the coal-fired generation capacity and provides back-up for renewable generation. APPrO submitted that reduced coal-fired generation will increase the runtime for gas-fired power generation.

APPrO submitted that Union's methodology to forecast power commodity revenue was fundamentally flawed since it used dated information. APPrO noted that Union included 2009, 2010 and part of 2011 data as the basis for the forecast and submitted that this was not appropriate as it did not take into account the impact of coal-fired generation closures. APPrO further maintained that Union did not incorporate the Independent System Electricity Operator ("IESO") forecast of a higher provincial power demand in 2013. The IESO 18-month outlook indicates that the 2013 aggregate energy consumption is expected to be 1.1% higher in 2013 than in 2011. In reply, Union submitted that customers were in the best position to provide relevant information. Union argued that customers ultimately have to contract for the services and it was in their best interest to provide reliable estimates.

APPrO submitted that commodity revenues for power customers for 2013 should be increased by $1.0 million which would be similar to the $4.9 million revenue collected from this group in 2011. This adjustment would also impact the customer supplied fuel which is treated as a revenue item by Union. APPrO submitted that customer supplied fuel should be increased by the same proportion as the commodity revenues which was 11% in this case. An 11% increase to customer supplied fuel results in an increase of $0.14 million to the $1.3 million included in rates.

With respect to overrun revenues, APPrO, LPMA, Energy Probe and Board staff submitted that Union had understated overrun revenues for 2013.Intervenors and Board staff submitted that Union had not forecasted any overrun charges in the power market for 2012 and 2013. This is despite the fact that the Halton Hills power plant had already incurred $300,000 in overrun charges up to the end of June 2012. Board staff suggested an increase of $300,000 to the overrun charges while LPMA submitted that the overrun revenue forecast for the power market should be adjusted to the same level as in 2011 which was $600,000. SEC and FRPO adopted LPMA's submission in this regard. Energy Probe submitted that the overrun revenues for the power market should be increased to about $500,000. APPrO submitted that the closure of the coal plants

and the low efficiency Lennox plant is driving additional volumes at Halton Hills and other gas-fired generation plans. APPrO therefore argued that 2012 overrun revenues could exceed 2011 revenues. APPrO proposed that the 2013 overrun revenue should be increased to $750,000 for 2013.

With respect to the non-power markets, LPMA expressed a concern about unsupported reductions in the overrun forecast. Union forecasted $600,000 in overrun revenues for the Test Year. LPMA noted that average overrun revenues for the non-power markets from 2007 through to 2011 were $1.7 million a year and have been stable over this period. LPMA submitted that $1.7 million was a reasonable forecast for 2013. Board staff, SEC and FRPO agreed with LPMA. APPrO noted that the three-year average overrun revenues in the non-power market which included 2007, 2010 and 2011 but excluded the financial crisis years of 2008 and 2009 was $1.8 million. APPrO accordingly submitted that the overrun revenues should be increased by $1.2 million which was $100,000 more than what the other intervenors had suggested.

In reply, Union submitted that it had forecast overrun revenues for 2013. Union noted that an amount of $600,000 related to overrun revenues had been included in 2013 rates.

Board Findings

The Board does not accept the contract customer demand forecast to be reasonable. As outlined below, Union’s forecasts do not reflect known changes in the market and environment, and have been demonstrated through evidence to be understated. The Board finds that the following three adjustments to Union’s contract customer demand forecast should be made.

First, with respect to commodity revenues, in preparing its forecast, Union considered only a narrow range of inputs, namely, its own forecast and estimates provided by each customer. In addition, the data is dated and does not take into account recent events or changes in the market. The Board agrees with APPrO that market conditions have changed significantly over the past couple of years because coal-fired generation is on the decline and is being replaced by gas-fired generation. Accordingly the Board directs Union to increase forecast 2013 commodity revenues by $1.0 million and directs

that a corresponding increase of $0.14 million in the fuel commodity revenue should also be made.

Second, the Board directs Union to increase forecast 2013 overrun revenues by $0.5 million. The Board notes that the evidence in the proceeding shows that actual power plant overruns in 2012 were already $0.3 million by mid-2012. There is no evidence to suggest that there would not be a continuation of such revenues in 2013.

Third, the Board directs Union to increase non-power market overrun revenue by $1.1 million from $600,000 to a total of $1.7 million in 2013, which is about the average revenue in this category from 2007 to 2011, exclusive of 2008 and 2009, the years of the financial downturn.

Storage & Transportation Revenue

Union's storage and transportation ("S&T") revenue forecast for 2012 and 2013 is organized under the following headings:

- Long-term transportation revenue forecast;
- Short-term transportation and exchanges revenue forecast; and
- Short-term storage and balancing revenue forecast.

Long-Term Transportation Revenue Forecast

Union's forecast for long-term transportation revenue is $148.5 million in 2012 and $141.9 million in 2013. The forecast is made up of three components: M12 Long-term Transportation, Other Long-Term Transportation, and Other Storage and Transportation Services.

M12 Long-term Transportation

The revenue for M12 Long-term Transportation represents long-term firm transportation on Union's Dawn-Parkway transmission system. It includes M12, M12X and F24-T transportation services which transport gas supplies easterly, westerly or bi-directionally on the system. Table 1 provides the actual and forecast revenues for M12 Long-term Transportation.

Table 1
M12 Long-term Transportation Revenue

Revenue (Millions)	2010 Actual	2011 Actual	2012 Forecast	2013 Forecast
M12 Transportation	$141.9	$138.3	$134.0	$121.1
M12 Transportation Overrun	$0.5	$0.0	$0.0	$0.0
M12X Transportation	$0.0	$1.5	$5.9	$13.5
Total	$142.4	$139.8	$139.9	$134.6

LPMA in its submission observed that as per Exhibit J.C-4-5-2, revenues for M12 long-term transportation revenues have been steadily increasing since 2007. LPMA noted that revenues for 2011 and the forecast for 2012 were just under $140 million, with a reduction of $5.3 million forecast for 2013 relative to 2012. LPMA further noted that as per Exhibit J6.3, the year-to-date actual revenues were tracking close to the forecast in 2012.

LPMA accepted Union's explanation of a reduction in 2013 which attributed the reduction to turnback of M12 capacity that began in 2011 and is forecast to continue in 2012 and 2013. LPMA noted that in a response provided in Exhibit J8.10, Union indicated that there was an increase of $280,000 based on changes to M12, M12-X and C1 long-term firm contracts since the forecast was completed. LPMA submitted that this increase should be reflected in the forecast.

LPMA submitted that an acceptance of the forecast did not imply that the capacity that was not currently contracted for had no value. LPMA submitted that Union had significant excess capacity on the Dawn to Parkway system and it was possible that the unused capacity may be contracted for in 2013. LPMA therefore submitted that any variance from the Long-term Transportation revenue forecast, both up and down, should be captured in a variance account and shared 90% to ratepayers and 10% to the shareholder. FRPO and APPrO adopted LPMA's recommendations on this matter. CME accepted LPMA's recommendation of a variance account but submitted that the actual amount in 2013 rates should be $139.8 million as compared to $134.6 million. CME

submitted that there was significant revenue potential considering that the gas had to get to Dawn regardless of where the gas was coming from.

In reply, Union rejected CME's proposal to adjust the M12 Long-term Transportation revenues. Union reiterated that it had experienced significant turnback on the Dawn-Parkway and Dawn-Kirkwall systems and this has resulted in a lower forecast in 2013 as compared to 2011 and 2012. Union also rejected LPMA's position that a deferral account should be established to capture the variance related to the Long-term Transportation revenue forecast. Union submitted that it has always been at risk for the Long-term Transportation revenues and that the same regulatory treatment should be continued.

Other Long-term Transportation

There are three components that comprise the Other Long-term Transportation revenue forecast: C1 Long-term Transportation, M13 (Local Production) and M16 (Storage-Transportation Service). The actual and forecast revenues for these services are shown in Table 2.

Table 2
Other Long-term Transportation Revenue

Revenue (Millions)	2010 Actual	2011 Actual	2012 Forecast	2013 Forecast
C1 Long-term Transportation	$6.3	$7.6	$6.6	$5.2
M13 Transportation	$0.4	$0.3	$0.4	$0.4
M16 Transportation	$0.6	$0.6	$0.6	$0.6
Total	$7.3	$8.5	$7.6	$6.2

Union attributed the decline in C1 Long-term Transportation revenue since 2011 to changes in market dynamics and gas flows affecting the Dawn-Parkway and Ojibway systems.

LPMA in its submission accepted the decline in C1 Long-term transportation revenues but noted that actual year-to-date 2012 revenues were up by 7% as compared to the

forecast. Accordingly, LPMA submitted that the 2013 forecast should be adjusted by the same proportion resulting in an increase of $400,000.

In reply, Union rejected LPMA's submission to make an upward revision of $400,000 to the C1 Long-term Transportation revenue forecast. Union provided the clarification that revenues for 2012 which were categorized as C1 short-term were actually sold as C1 long-term. Consequently, there was an increase in the C1 Long-term Transportation forecast and a decrease in the C1 short-term transportation forecast. Union further submitted that this was an example of a selective adjustment where LPMA proposed adjustments for positive variances but excluded adjustments when they showed a negative variance.

Union submitted that the overall forecasts were reasonable even though there may be some negative or positive variances in the different categories. With respect to C1 Long-term Transportation, Union indicated that Dawn to Parkway revenues were offset by the negative variance in the M12 account. Union submitted that it had essentially forecast more capacity to be sold as short-term firm rather than C1 long-term.

Other S&T Revenue

This category is comprised of revenue earned from name changes, Ontario Producers and other miscellaneous services. The revenue for these services have been constant at $1.1 million in 2010 and 2011 and forecasted to be the same for 2012 and 2013. LPMA accepted Union's forecast for these services. APPrO and FRPO adopted LPMA's submission with respect to Long-term Storage and Transportation Revenue.

Board Findings

The Board accepts Union's forecast of 2013 M12 Long-Term Transportation Revenue, Other Long-Term Transportation Revenue, and Other S&T Revenue as reasonable. The Board will not require Union to adjust estimated revenues as was suggested by some parties, as the Board concurs with Union that the adjustments are selective in nature. The Board rejects LPMA's request to establish a variance account related to Long-term Transportation Revenue, as the Board believes that Union should continue to bear this forecast risk, consistent with the current treatment.

Short-term Transportation and Exchanges Revenue Forecast

The short-term transportation and exchanges revenue forecast is $32.2 million for 2012, and $20.2 million for 2013.

Short-term Transportation

The transportation component of the transactional forecast is comprised of short-term firm and interruptible transportation on Union's Dawn-Parkway systems, the Ojibway system and St. Clair/Bluewater system. Union forecasted $11.1 million in revenues in 2012 and again in 2013, down from $12.5 million in 2011. Union attributes the decline to insufficient takeaway capacity on TCPL downstream of Parkway. LPMA in its submission accepted the forecasted declines. LPMA also argued that the same variance account treatment that it proposed for Long-term Transportation Revenues should be applied to Short-term Transportation Revenues.

Board Findings

The Board accepts Union's forecast of 2013 Short-term Transportation Revenue as reasonable. The Board rejects LPMA's request to establish a variance account related to Short-term Transportation Revenue, as the Board believes that Union should continue to bear this forecast risk, consistent with the current treatment.

Short-term Storage & Balancing

Union's forecast for short-term storage and balancing is $9.1 million in 2012 and $11.5 million in 2013. This forecast is comprised of two components: peak short-term storage, and off-peak storage, balancing and loans. Union has forecasted an increase in 2013 related to short-term peak storage revenues. The primary reason for this increase is the increase in the forecast price of storage, from $0.55 per GJ in 2012 to $0.85 per GJ in 2013.

LPMA noted that based on data provided in Exhibit J6.3, the June year-to-date revenues for off-peak storage/balancing/loan services were tracking close to the forecast. LPMA accepted Union's forecast for 2013 since 2012 revenues were on track to meet the forecast and the forecast of $2.5 million for 2013 was similar to 2012.

However, LPMA noted that according to Exhibit J6.3, the year-to-date revenues for short-term storage services were over the forecast by $2.7 million, i.e. 87%. Moreover, the June 2012 actual revenues of $5.8 million were only slightly under the annual forecast of $6.6 million. LPMA submitted that using the same methodology as for base exchanges, the projected 2012 forecast based on how revenues were currently tracking was $12.3 million.

LPMA submitted that the 2013 forecast should be increased to the projected 2012 level of $12.3 million from the current forecast of $8.988 million. LPMA noted that the forecast of $12.3 million was still below the levels recorded in 2007 through 2010, despite more excess utility space projected to be available in 2013 than in previous years. FRPO and CME agreed with LPMA on these issues.

In reply, Union submitted that the 2012 forecast was initially prepared at an average price of $0.55 per GJ. However, the actual price was $0.84 per GJ and this was the cause of the positive variance. Union provided clarification that the forecast for 2013 was based on actual 2012 prices, which were at $0.60 per GJ and not $0.85 per GJ. Union submitted that there was no evidentiary basis to increase the 2013 forecast.

Board Findings

The Board accepts Union's forecast for 2013 Short-Term Storage & Balancing revenue as reasonable. Given the uncertainty relating to the forecast, the Board approves the continued operation and use of the Short-Term Storage & Balancing variance account to capture any variance of Short-Term Storage & Balancing net revenue from forecast, both up and down during the 2013 test year, consistent with the current practice. The Board notes that 90% of the net revenue forecast related to short-term storage and balancing is to be built into rates for 2013. The balance in the variance account is to be shared 90% to ratepayers and 10% to the shareholder.

OPTIMIZATION AND GAS SUPPLY PLAN

Exchanges

Exchange revenue is comprised of activity using Union's upstream transportation capacity to provide exchange services to third parties. It also includes net revenue generated from pipe releases or revenue from TCPL's Firm Transportation Risk Alleviation Mechanism ("FT-RAM") program. Union did not include any amount for the FT-RAM program in its Application due to the uncertainty surrounding the continuation of the program. TCPL has proposed to end the program in its current application before the National Energy Board.

Union included base exchange related revenues of $9.1 million in 2013. This compares to $8.6 million in 2010, $9.7 million in 2011 and a forecasted amount of $6.9 million in 2012.

LPMA and Energy Probe submitted that the forecast for base exchange revenues were significantly understated. LPMA referred to Exhibit J6.3 which shows that the actual base exchange revenue for year-to-date as at the end of June was 66% higher than the forecast for the same period. LPMA proposed that the Board should increase the 2013 forecast of $9.1 to reflect the under forecast in 2012. Union forecasted achieving $4.0 million or 58% of its revenues as of June 2012. LPMA proposed using the same ratio but applying it to the actual revenues of $6.6 million as of June which would result in an annual number of $11.4 million for 2012. LPMA submitted that Union had provided no evidence that base exchange revenues would decline in 2013 and the Board should therefore increase Union's revenues from $9.1 to $11.4 million in 2013, essentially maintaining the same level as that projected for 2012. CME supported LPMA's submission in this matter.

Union, in its reply argument, submitted that the Board should include $9.1 million in rates for base exchanges with any variance subject to sharing 75:25 in favour of ratepayers, consistent with the treatment prior to IRM.

Firm Transportation Risk Alleviation Mechanism ("FT-RAM")

FT-RAM or Firm Transportation Risk Alleviation Mechanism is a service to TransCanada's long-haul firm transportation ("FT") shippers. The FT-RAM program allows long-haul FT shippers to apply unutilized FT demand charges against their cost of interruptible transportation ("IT") service. TCPL introduced the FT-RAM program to promote the renewal of incremental contracting for long-haul FT service.

In its Argument-in-Chief, Union proposed to include $11.6 million in rates and establish a variance account to capture any additional revenues or any revenue shortfall. Union submitted that it should have 100% downside protection below $11.6 million and any revenue above $11.6 million should be shared 75:25 in favour of ratepayers.

Energy Probe submitted that Union's forecast of $11.6 million should be accepted only if the Board categorizes these revenues as transportation related. Energy Probe submitted that FT-RAM revenues should be classified as gas costs and 100% of the revenues should go to ratepayers through the Purchased Gas Variance Account.

Board staff submitted that Union had used the capacity that is excess to its gas supply plan to generate a significant amount of revenue over the years. In cases where the transportation capacity was assigned to a third-party, Union earned revenue by selling this capacity. Revenues generated through assignments flowed to ratepayers through the Unabsorbed Demand Charges ("UDC") deferral account. However, when Union needed the supply and it was being delivered through an alternate route, revenue generated as a result of such assignment flowed to Union's utility earnings. If the empty pipeline was TCPL capacity, then Union generated RAM credits through TCPL's FT-RAM program. Board staff submitted that under the FT-RAM program Union was monetizing RAM credits and it was then delivering gas through alternate and cheaper routes. In other words, Union was selling transportation capacity paid for by ratepayers and repurchasing the same service at a lower cost while keeping the margins. Board staff along with a number of intervenors submitted that Union had generated significant revenues using the FT-RAM program during the IRM period, the majority of which flowed through to Union's shareholder.

Board staff submitted that almost all revenues generated as a result of using pipeline capacity that customers have paid for in gas supply costs should go back to offset gas

costs. Board staff submitted that customers have paid for this capacity and they should therefore derive any benefit as a result of optimization. However, Board staff did recognize that Union needs some incentive to optimize and proposed that 90% of the revenues generated through optimization activities related to transportation capacity that in-franchise customers have paid for should go to offset gas costs while the remaining amount should flow to utility earnings.

Although most intervenors agreed with the general argument of Board staff, they rejected the sharing formula. Intervenors such as LPMA, BOMA, Energy Probe, CME and FRPO submitted that all revenues generated through optimization activities related to transportation capacity paid for by ratepayers should go to offset gas costs. LPMA submitted that Union should not receive any incentive to get the best cost for the gas it supplies to its system gas customers. LPMA noted that Union does not make a profit on the cost of gas; it is a flow through cost to system gas customers. LPMA submitted that the cost of gas includes the cost of getting the gas to the Union system. LPMA stressed that the actual cost of gas, including the actual cost of getting it to Union is what system gas customers should be paying for. APPrO adopted LPMA's submission with respect to exchange related revenues.

FRPO in its submission attempted to provide some distinction between revenues that should offset gas costs and revenues that represent true optimization. FRPO submitted that FT-RAM credits associated with long haul contracts should be classified as gas costs while optimization of transportation within Union's franchise area or optimization of Storage Transportation Service ("STS") contracts could be classified as optimization that would be captured in the historical storage and transportation exchange services deferral account.

CME in its submission addressed the larger issue of revenue deficiency noting that cumulative overearnings during the IRM years averaged around $40 million a year. CME submitted that it could not understand why ratepayers were facing a revenue deficiency as opposed to a sufficiency. CME attributed the overearnings during the IRM years to revenue increases rather than cost reductions. An important contributor to the revenue increases was FT-RAM revenues.

CME noted that the Board and intervenors rely on Union to adhere to the concepts and principles embedded in the Board's regulation of gas utilities. CME submitted that one

of the fundamental concepts was that for ratemaking purposes, gas commodity costs and upstream transportation costs are to be treated as pass-through items. CME maintained that the utility should neither profit nor lose as a result of the actual commodity or upstream transportation costs. CME was of the opinion that the utility holds the amounts in trust that it receives from ratepayers on account of gas commodity or upstream transportation costs. If actual costs are less than the actual amounts collected, then ratepayers are to receive a credit and if actual costs are higher, then ratepayers have to pay the difference. CME submitted that the excess funds could not be converted to profits without the prior explicit consent of ratepayers or the utility regulator.

CME submitted that Union had not presented all the relevant facts for the intervenors and the Board to determine the validity of its actions. CME maintained that Union's argument that it has undertaken optimization activities before is irrelevant since it had never explicitly presented the facts to the Board. CME asserted that Union could not unilaterally take action to enrich its shareholder at the expense of ratepayers.

In its Argument-in-Chief, Union indicated that there was a deferral account relating to upstream optimization and exchange activity going back to 1993 and perhaps even earlier. Union submitted that the exchange activities Union has undertaken since 2003 as it related to FT-RAM were similar to optimization activities that it undertook before and would undertake in 2013. Union referred to an interrogatory response that states that Union was able to extract value from new services introduced by upstream transportation providers in excess of what was achieved historically.[7] The new service referred to was TCPL's FT-RAM.

CME, in its submission, rejected Union's argument that FT-RAM refers to activities that are covered by the existing deferral accounts related to upstream transportation and exchange activities. CME stressed that the deferral accounts referred to only that component of upstream transportation that was periodically freed up as a result of weather or declines in demand. The rationale for sharing the incentive between the utility and ratepayers was to facilitate the use of idle capacity.   CME submitted that this account did not cover optimization of upstream transportation surpluses self-created by the utility on a planned basis.

[7]CME Final Argument at Tab 28,

CME in its submission noted that there were two means through which Union monetized FT contracts. One was through capacity assignments and the other one was through leaving its FT capacity unutilized and using a cheaper alternative route to transport the required gas. CME submitted that both of these activities were nothing but upstream gas cost reductions. They could not be classified as exchange transactions or a transactional service. CME maintained that these were planned decisions and not related to capacity temporarily rendered surplus due to conditions beyond Union's control, such as weather or demand. CME submitted that revenues generated as a result of such activities must be classified as gas costs and should be cleared through the current regime of gas supply deferral accounts.

LPMA submitted that should the Board determine that FT-RAM revenues should not flow to system gas customers, but should flow through S&T revenues, then the amount included in the forecast for 2013, and how it is allocated to rate classes needed to be addressed.

LPMA noted that Union had proposed to include $11.6 million in rates, with a variance account to provide protection. LPMA referred to Exhibit J7.11 that estimated FT-RAM revenues of $37.8 million should the program continue for all of 2012. LPMA also noted that Union had received FT-RAM credits of $19.9 million on a year-to-date basis.

LPMA submitted that the Board should not approve the inclusion of any amounts in rates for 2013. In this way, customers would receive some credit in 2013 and would not be faced with a claw back if the program was eliminated. LPMA further noted that such an approach would eliminate the need to determine how to allocate the credits to the various rate classes. The allocation could be dealt with in a later proceeding when the credits came up for disposition. IGUA recommended a similar approach because it did not support including FT-RAM revenues as a rate mitigation option considering that it may not be available in 2013 and beyond. However, IGUA did not take any position on the treatment of FT-RAM revenues.

In reply, Union disagreed with the categorization proposed by intervenors. Union noted that intervenors were attempting to make a distinction between RAM-related exchanges and base exchanges with their argument being that RAM-related revenues should offset gas costs while base exchange revenues should be treated as traditional S&T revenues. Union argued that an exchange was an exchange and that there was no

distinction to be made. Union saw no reason to depart from the well-established regulatory treatment of exchanges that treats them as regulated revenues pursuant to the C1 rate schedule.

Union also observed that exchange revenues were not unregulated. The only difference was that during the IRM period they were not subject to deferral treatment. However, they continued to be part of the utility earnings calculation and were subject to earnings sharing.

Union reiterated the definition of an “exchange” that had been clarified several times during the proceeding. Union stated that:

> An exchange is a contractual agreement where party ‘A’ agrees to give physical gas to party ‘B’ at one location and party ‘B’ agrees to give physical gas to party ‘A’ at another location. Either party ‘A’ or party ‘B’ may agree to pay the other party for this service. An exchange can only happen between a point on Union’s system and a point off of Union’s system. The exchange must also happen on the same day at the same time.

Union also rejected the argument of intervenors that the exchange activities were planned and a feature of the gas supply plan. Although Union forecasted a certain level of activity, Union submitted that it was consequential to the service made available by other parties, specifically TCPL.

Union, in reply, noted that the gas supply deferral accounts and the S&T deferral accounts have existed in parallel for years and the treatments for these deferral accounts have been different. While the gas supply deferral accounts have been treated as pass through items, exchanges and other S&T related activities have been treated as forecast revenues subject to deferral treatment.

Union also rejected CME’s assertion that the Board had no knowledge of Union’s FT-RAM related activities prior to this proceeding. Union submitted that in the EB-2009-0101 proceeding, Union explicitly informed parties that it had taken advantage of the FT-RAM service offered by TCPL. During this proceeding, Union reported significant over-earnings in relation to its S&T forecast. Union stated that in response to the over earnings, intervenors revised the 2007-0606 IRM settlement agreement and changed

the earnings sharing mechanism from 50:50 to 90:10 in favour of ratepayers to be triggered if the actual ROE exceeded the Board approved ROE threshold by 300 basis points.

Union stressed the fact that intervenors had the opportunity to review whether IRM should continue or not in the EB-2009-0101 proceeding when Union crossed the 300 basis points threshold, but they chose not to. Union pointed to the fact that it was evident that a large contributor to the over earnings was Union's S&T activity that contributed $37 million to earnings of which Union's use of FT-RAM was a significant component.

Union also referred to the 2009 rates proceeding (EB-2008-0220), wherein the Board rendered a decision on a new service introduced by TCPL, Dawn Overrun Service – Must Nominate ("DOS MN"). In this proceeding, CME argued that DOS MN related revenues should be treated as gas supply costs. The Board did not agree with CME and determined that DOS MN revenues should be treated as S&T revenues. Union submitted that although DOS MN and FT-RAM were different services, the treatment was the same.

Union argued that it needs to sell an exchange into the market under the C1 rate schedule and this results in revenue being generated. Union therefore submitted that these revenues cannot be categorised as gas costs because they do not fit in either the gas commodity reductions or toll variances categories.

Union rejected intervenors' position and submitted that intervenors are attempting to classify revenues between gas costs and traditional S&T activity. Union argued that CME's definition did not take into account the market and it was not feasible to monitor the weather or demand on a daily basis. With respect to FRPO's definition, Union indicated that it was limited to particular services and would not be applicable if Union's portfolio were to change from long-haul to short-haul services or if it were to earn revenues on the Dawn-Parkway system.

Union submitted that the best approach would be to establish an exchange-related account that is subject to sharing. This would avoid the problem of trying to differentiate the revenues generated and would be a principle based approach that would simplify implementation on a going forward basis. Union indicated that it had estimated FT RAM

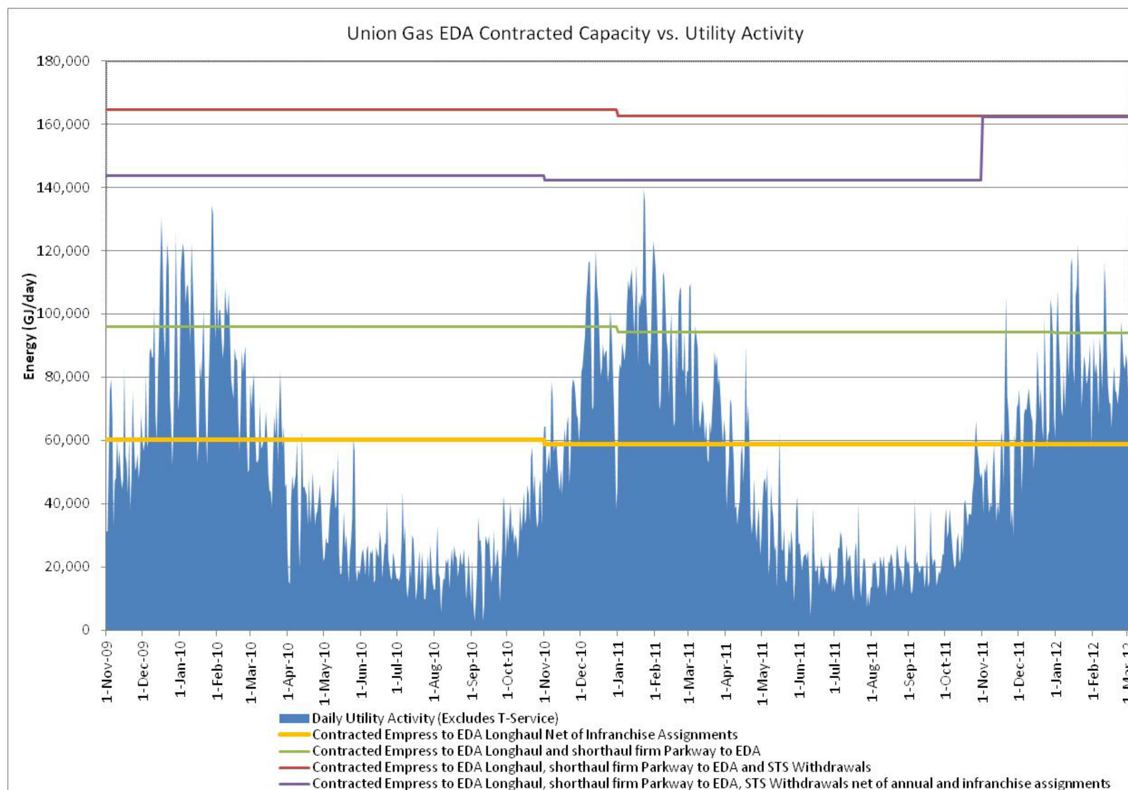
related revenues of $11.6 million in 2013. However, its preferred approach was to embed no amount in rates and have a deferral account that is subject to a 75:25 sharing in favour of ratepayers.

Gas Supply Plan

Union's gas supply planning process is guided by a set of principles that are intended to ensure that customers receive secure, diverse gas supply at a prudently incurred cost. Intervenors and Board staff submitted that Union is over contracting for FT Service to the Northern/Eastern Delivery Areas and this has resulted in customers incurring UDC for upstream transportation that is left empty or does not flow to full capacity to meet customers' annual firm demands. Board staff and Energy Probe submitted that ratepayers have incurred approximately $5.7 million in UDC costs from 2007 to 2011. Intervenors and Board staff further submitted that Union had arbitraged the excess firm capacity generating transportation revenues for the utility. Union, in reply submitted that all parties referred to the excess in a general manner and no party specifically identified the excess quantity or the specific contracts that Union should not have entered into.

Intervenors and Board staff referred to the graphical representation below of firm contracts in the Eastern Delivery Area ("EDA") that shows how the excess capacity of 20,000 GJ per day was assigned on a long-term basis. VECC, in its submission, noted that a portion of annual transportation contracts was assigned in its entirety on an annual basis, such that, from an operational perspective, it was as if Union had never entered into these contracts.[8]

[8] VECC Final Argument atp.20.



Referring to the same chart, Union, in reply, submitted that it did not over contract and the contracted capacity shown in the chart was appropriate in order to meet a design day. Union further noted that during the valley periods, Union injects gas into storage in order to meet average utility consumption throughout the year. If Union did not inject gas into storage then it would need to contract for even more gas and thus more capacity, during the winter. Union submitted that intervenors did not provide any support for their argument that Union had excess upstream capacity apart from the fact that Union earned S&T revenues during that period. Union submitted that ultimately the gas was required to meet in-franchise customer needs as presumed in the gas supply plan.

Board staff argued that Union's reliance on a design day[9]that is based on the coldest day within the past 50 years is flawed and this results in a far larger cushion than required. In its reply submission, Union argued that Union's design day of minus 29 degrees Celsius was not extremely cold for some of Union's service areas such as Fort Francis and North Bay. Union further noted that although Union's franchise area last experienced the design day in 1981, it has had several days of extreme weather where

[9] Oral Hearing Transcripts, EB-2011-0210, Volume 7 at pp. 161-162. (Design Day is a 47 degree day in the North and a 44 degree day in the South).

the temperature has been within two heating degree days of the design day. Union submitted that the importance of design day is critical in utility planning because the consequences of not having gas on a design day could be significant.[10]

Board staff and VECC noted that Union confirmed at the hearing that if the actual degree day requirements had exceeded the capacity of the firm assets that remained after optimization, Union would have been able to meet its gas supply requirements in several ways. Consequently, Board staff and VECC argued that Union did not require the capacity that it had contracted for. Union in its reply argument noted that its transportation portfolio had been adjusted substantially downwards since 2000. Union submitted that between 2002 and 2011, Union had reduced its long-term firm transportation portfolio of Empress to the Northern Delivery Area by 47%, from 358,643 GJs per day to 191,177 GJs per day.

CME submitted that a gas supply plan that was premised to profit from using upstream transportation capacity paid for by ratepayers was incompatible with the principle that a utility cannot profit from amounts received for upstream transportation.

FRPO, in its submission, argued that Union's gas supply plan relies on long-term firm service contracts that have been avoided or turned back by all customers, including prudent utilities in Canada and the United States within the last few years. FRPO indicated that declining firm contracts on the TCPL mainline is common knowledge. However, Union has continued to hold annual FT contracts even though utilities like Enbridge have moved to shorter-term arrangements such as winter Short-Term Firm Transportation ("STFT"). FRPO referred to Union's response at the hearing that expressed the possibility that Union may not be able to recontract if it were to move to winter STFT. However, FRPO argued that firm contracting on the TCPL main line has diminished significantly, resulting in spare capacity that cannot be sold.

In its reply argument, Union submitted that it had turned back substantial quantities of long haul FT Service during the past few years. Union noted that unlike Enbridge, Union does not require winter peaking service and therefore the reference by FRPO to Enbridge's winter STFT service was not relevant. Union also disputed FRPO's claim that STFT service has always been available and with the exception of service to

[10]Oral Hearing Transcripts, EB-2011-0210, Volume 16 at p.85.

Montreal, STFT has been available for decades. Union submitted that it had indicated at the hearing that STFT was not available in 2011 in the Sault Ste. Marie Delivery Area. In addition, if Union were to use STFT service to get gas in the Sault Ste. Marie Delivery Area, it would have to ensure that STFT was available on all three segments, Dawn to St. Clair, the international crossing and from St. Clair to Sault Ste. Marie. For these reasons, Union submitted that it did not contract for STFT.

CME expressed concerns related to the forecast of 10.4 PJs of UDC which was significantly higher than the current forecast of 4.4 PJs. CME's concern was related to the fact that the UDC for Union was increasing while the market as a whole was taking steps to minimize expected UDC through a combination of FT and STFT. CME submitted that Union was not taking any steps to minimize UDC.

CME submitted that Union should be directed to mitigate the level of UDC to the maximum extent possible with the condition that the Board would review the UDC amount in a future process. CME did not suggest making any changes to the forecast UDC.

VECC, FRPO, CME and LPMA submitted that the Board should require a consultation that includes Union and interested parties to review and recommend changes to the gas supply plan that better responds to the needs of ratepayers. However, many intervenors agreed with Board staff that the gas supply plan for 2013 should be accepted. IGUA did not take any position on the gas supply issue.

Union, in reply, submitted that the gas supply plan was prudent and should be approved as filed. The principles were reasonable and the Board has on previous occasions approved Union's gas supply plan with no changes. Although Union did not feel that a consultation was required, it did indicate that should the Board decide to consider this approach, Union would prefer an independent review as compared to a consultation with intervenors.

Board Findings

Although the issues of optimization and natural gas supply planning are listed separately on the Issues List, it is evident to the Board from this proceeding that the issues are, in fact, inter-related.

Union defines optimization as a market-based opportunity to extract value from the upstream supply portfolio held by Union to serve in-franchise, bundled customers. Union asserts that exchanges are nothing more than a type of optimization activity. Union has defined an exchange as a contractual agreement where party A agrees to give physical gas to party B at one location, and party B agrees to give physical gas to party A at another location. Either party A or party B may agree to pay the other party for this service. An exchange can only happen between a point on Union's system and a point off Union's system.

It is clear to the Board that the nature of Union's optimization activities has evolved since the NGEIR proceeding[11] and the commencement of Union's incentive regulation regime. Union has submitted in past proceedings that in the context of a balanced gas supply portfolio, few if any, firm assets are available to support transactional services on a future planned basis[12]. Union has asserted that firm assets are made available as a result of weather and market variances.

The Board finds that the record in this proceeding is clear that firm assets are being made available for transactional services on a planned basis, with releases occurring prior to the commencement of the heating season and with capacity being assigned for up to a full year. The revenues or margins arising from these services are not being returned to customers as an offset to gas supply costs.

The Board observes Union's statements that the purpose of the gas supply plan is to ensure secure and reliable gas supply to bundled customers from a diverse supply range, all at a prudently incurred cost. However, the record in this proceeding suggests that Union's optimization activities have, in their own right, become a driver of the gas supply plan, and are no longer solely a consequence of it.

The Board finds that Union's ability to "manufacture" optimization opportunities undermines the credibility of Union's gas supply planning process, the planning methodology, and the resulting gas supply plan.

[11] The Board initiated the Natural Gas Electricity Interface Review ("NGEIR") in 2005 to examine the regulatory treatment of natural gas infrastructure and services, specifically storage regulation (EB-2005-0551).
[12] RP-2003-0063/EB-2003-0087, Exhibit C1, Tab 3, Page 6 of 16.

As submitted by various parties to this proceeding and Board staff, Union has had an incentive to contract excessive upstream gas transportation services to the detriment of the ratepayer. Union has not filed convincing evidence that the amount and type of upstream gas transportation contracts procured on behalf of ratepayers reflects the objective application of its gas supply planning principles.

For example, the Board is of the view that the schedule filed by Union[13] showing decontracting on the TCPL system is not helpful. The schedule does not inform the Board's overall assessment of whether the gas supply plan is prudent, as the schedule does not speak to whether too much or too little TCPL capacity has been released. Further, the schedule does not inform the Board as to whether the increase in tolls on the remaining long-term FT capacity with TCPL arising from decontracting has been more than offset by reductions in tolls on alternative transportation routes, including those pipeline companies in which Union's parent company has, or will have, an economic interest.

Union provided evidence that it did not consider this type of cost-benefit analysis in its gas supply planning function and that the gas supply personnel look only at current tolls when making a purchasing decision.[14] Moreover, Union testified that its gas supply planning personnel may not have an understanding of the basis upon which the rates or tolls paid for upstream transportation are calculated.[15]

The Board does not accept this approach. The Board is of the view that the principles used by Union's gas supply planning group are at a very high level and thus provide little guidance with respect to how the costs that Union incurs are calculated, and whether such costs would, in fact, be prudently incurred.

Union's evidence on its optimization activities has not been clear and Union's approach with respect to optimization in general has not been helpful. The Board notes that absent the TCPL application filed with the NEB on September 1, 2011, little information describing the nature of these activities (notably FT-RAM) would have been available.

In RP-1999-0001, the Board, quoting from E.B.R.O. 452 (paragraph 6.5 of that decision) stated that:

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[13] Union Gas Reply Argument Compendium, Gas Supply Tab 4. Union Gas – TransCanada Long-haul and STS Summary 2000 – 2011.
[14] Oral Hearing Transcripts, EB-2011-0210, Volume 3 at pp. 103-104.
[15] Ibid. at pp. 153-155.

> Regulation is intended to be a surrogate for competition in the marketplace and the legislation intended that the Company has an opportunity to recover its costs and to earn a fair rate of return on its shareholders' equity…The system requires the regulator to act on faith with the utility, bearing in mind the prospective nature of the evidence. The regulator expects the utility, in return, to provide the best possible forecast data that can be made available, on a timely basis.

The Board also said in paragraph 4.2 of RP-1999-0001:

> The Board appreciates that business plans are not carved in stone and the utility must have flexibility to meet ongoing demands of the marketplace; however, this flexibility must be balanced against the utility's obligations as a regulated entity. This is particularly true when the Company is not responding to exogenous events, beyond the Company's control, but is implementing its own initiatives.

Union stated that there have been at last 20 separate proceedings before the Board relating to QRAMs, deferral accounts, and rebasing and argued that the Board's discovery-related powers are tools that the Board has at its disposal which go well beyond what even a court of law has in a civil context. The implication of these arguments is that these issues should have been identified by intervenors and Board staff via interrogatories, document production, and technical conferences.[16]

The Board disagrees with Union's assertion that it is the responsibility of intervenors and Board staff to undertake adequate discovery to ensure that the record is complete. Union is a rate regulated entity, and the information asymmetry in evidence in this proceeding is illustrative of the need for the Board to reiterate Union's affirmative disclosure obligations.

At paragraph 4.5 in RP-1999-0001 the Board clearly sets out a utility's affirmative obligation to disclose by stating:

> The Company has an affirmative obligation to provide the Board with the best possible evidence and it is not incumbent on the intervenors to ensure, through cross examination of the Company's witnesses, that the record is adequate and complete. The Company cannot shirk its

[16] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at p. 3.

responsibilities as a regulated entity by submitting evidence that is vague and incomplete.

Union has not met this affirmative obligation.

Optimization

Consistent with the long-standing principle that a gas utility should not profit from the procurement of gas supply for its in-franchise customers, and to eliminate the creation of inappropriate incentives during the test year, the Board finds that the optimization activities, as defined below, are to be considered part of gas supply, not part of transactional services.

The Board reiterates that gas supply costs refer to both the upstream gas cost, including fuel gas, and the cost (rate multiplied by contract volume) of upstream transportation that is required to deliver gas supply to Union's in-franchise customers in the North and South Delivery Areas.

Consistent with the description provided by Union, the Board will define optimization as any market-based opportunity to extract value from the upstream supply portfolio held by Union to serve in-franchise bundled customers, including, but not limited to, all FT-RAM activities and exchanges.

The Board finds that 90% of all optimization net revenues shall accrue to ratepayers and 10% shall accrue to Union as an incentive to continue to undertake these activities on behalf of ratepayers. Although Union has undertaken optimization activities for a lengthy period of time, it has indicated that absent an incentive, these types of activities may not occur. The Board has not considered the issue of whether optimization is an integral part of prudent utility practice that should be undertaken by Union without the payment of an incentive. Absent consideration of this issue by the Board in the context of this proceeding, the Board is of the view that it is appropriate for an incentive to be continued, at a 10% rate. This level of incentive is consistent with that associated with short-term storage and balancing.

The Board orders the establishment of a new gas supply variance account in which 90% of all optimization margins not otherwise reflected in the revenue requirement are to be captured for the benefit of ratepayers. This variance account is symmetrical. The balance of this gas supply variance account will be disposed of on an annual basis.

The Board finds that at the time an application to clear this new gas supply variance account is filed with the Board, Union must also file a proposal to allocate the balance of the new gas supply variance account to in-franchise customers, including direct purchase customers in the North. This proposal must be based on regulatory principles.

Consistent with these findings, 90% of Union's 2013 forecast of base exchanges of $9.1 million is to be reflected in the 2013 test year revenue requirement. Union's 2013 forecast of FT-RAM related revenue is $11.6 million. Given the uncertainty relating to whether the FT-RAM program will be continued by TCPL through the 2013 test year and subject to the Board's finding that a 10% incentive for optimization activities is to accrue to Union, the Board finds that only half (50%) of Union's FT-RAM forecast for 2013 should be reflected in the 2013 revenue requirement. To be clear, 90% of one half of Union's estimate of FT-RAM related revenue in 2013 is to be reflected in Union's 2013 Board-approved rates, i.e. $5.22 million.

Gas Supply Plan

The Board approves Union's 2013 Natural Gas Supply Plan, as filed. However, the Board has concerns with Union's gas supply planning process, its planning methodology, and the resulting supply plan in light of Union's actions over the incentive regulation period. The Board believes that confidence in the gas supply plan is essential. The Board is therefore of the view that a further, more detailed review of Union's gas supply planning functions would be beneficial.

The Board is of the view that an expert, independent review rather than a consultation is a better way to proceed, given the highly specialized nature of the review to be undertaken. Accordingly, the Board orders Union, prior to its next rates proceeding (cost of service or incentive regulation), to file with the Board an expert, independent review of its gas supply plan, its gas supply planning process, and gas supply planning methodology.

This review is to be conducted by an independent third party with gas supply planning expertise. The Board directs Union to establish a deferral account to capture the cost of the expert, independent review, for disposition in Union's next rates proceeding.

As suggested by Union, intervenors and Board staff are to be provided an opportunity to review the Request for Proposals ("RFP") associated with this review prior to issuance. The scope or purpose of the review will be subject to the comments of intervenors and Board staff. In addition to comments that may be provided by parties, the Board finds that the purpose of the review should include, but not be limited to, the following:

1. Verify that Union's gas supply planning process, methodology, and plan reflects appropriate planning principles, including a reference to cost.
2. Determine whether planning principles are objectively applied and result in a gas supply plan that is "right sized".
3. Determine whether Union's differing peak-day methodologies in the North and South Delivery Areas are appropriate, and if not, recommend alternative approaches.
4. Recommend whether the two approaches should be aligned.
5. Compare the methodology of determining the peak design day, based on the coldest day in the last 50 years, with other heat-sensitive distributors in North America.
6. Determine whether the peak day in the North and South Delivery Areas are appropriately/consistently reflected in the gas supply plan, and if not, recommend remedial action.
7. Determine whether Union is conducting sufficient due diligence with respect to the cost benefit analysis associated with decontracting a particular gas transportation route and recontracting on an alternative route, and recommend remedial action, if required.
8. Determine whether Union is using the transportation portion of the gas supply portfolio to favour the transportation paths of entities in which Union or its parent has (or will have in the future) an economic interest, and recommend remedial action, if required.
9. Examine the cost allocation and rate design used by Union to allocate the cost of gas supply to in-franchise customers in the North and South to ensure that it is appropriate and reflects regulatory principles.
10. Examine the structure of the current natural gas supply deferral and variance accounts, with a view to simplifying and standardizing these accounts in the North and South Delivery Areas.
11. Determine whether the structure and text of the various natural gas supply deferral and variance accounts is consistent with the principles of the Decisions and Orders that provided the authorization for these accounts and consistent with the findings of the Board in this proceeding, and recommend remedial action, if required.

The results of the review are to be subject to a stakeholder information process and then be submitted in conjunction with Union's next rates proceeding (cost of service or incentive regulation regime).

COST OF CAPITAL

Union's investment in rate base is financed by a combination of short-term and long-term debt, preferred shares and common equity. The current Board approved capital structure is based on a 36% common equity component. The remaining 64% is financed by a mix of short-term debt, long-term debt and preferred shares.

Union has proposed a capital structure which includes a common equity ratio of 40% for 2013 as compared to the 36% currently included in rates. The 36% equity ratio was set as a result of a Settlement Agreement in the 2007 Cost of Service Proceeding (EB-2005-0520).

Union has proposed a long-term debt ratio of 60.17% and a debt rate of 6.53%. The short-term debt ratio is -2.92% with a rate of 1.31%. The average embedded cost of preferred share capital for 2013 is 3.05%. This is a decrease from the 2007 Board approved cost of 4.74%.

Common Equity Ratio

Most intervenors and Board staff submitted that Union's proposal to raise the common equity ratio from 36% to 40% should be rejected. IGUA did not take any position on this issue.

In support of its proposal, Union retained two experts: Mr. Steven M. Fetter and Dr. Vander Weide. In response, intervenors presented the expert evidence of Dr. Lawrence D. Booth.

Intervenors and Board staff cited the Report of the Board on Cost of Capital for Ontario's Regulated Utilities[17] that provided guidelines with respect to a gas utility's capital structure. The report on page 50 states:

[17] Report of the Board on Cost of Capital for Ontario's Regulated Utilities, dated December 11, 2009 (EB-2009-0084),pp. 49, 51.

> For electricity transmitters, generators and gas utilities, the deemed capital structure is determined on a case-by-case basis. The Board's draft guidelines assume that the base capital structure will remain relatively constant over time and that a full reassessment of a gas utility's capital structure will only be undertaken in the event of significant changes in the company's business and/or financial risk.

Intervenors and Board staff submitted that Union had made no attempt to comply with the guideline in requesting a change in the equity thickness and Union's evidence indicated that it had not analyzed its financial and business risk as part of this proceeding. Board staff and intervenors further noted that Union's argument was that its current equity structure is not commensurate with its risk. However, Union agreed that its business or financial risk had not changed materially since 2006. In fact, Union witnesses confirmed several times during the oral hearing that there had been no material increase to its business or financial risk.[18] Union agreed in reply that its risk profile had not changed but it noted that in the 2007 rates case, Dr. Carpenter and the Brattle Group stated that Union's business risk warranted an equity ratio between 40 and 56%, depending on the allowed rate of return.[19] Union therefore believed that an equity ratio of 40% was appropriate based on its current risk profile.

Mr. Fetter was of the opinion that an equity thickness of 40%-42% would improve Union Gas' financial profile benefitting its customers through Union's enhanced ability to attract capital from investors when needed and upon reasonable terms. Mr. Fetter, in his report, also indicated that equity ratios of utilities were rarely set below 40% in the United States. Mr. Fetter further noted that a review of other Canadian gas utilities showed that the deemed equity ratios were in the range of 39% to 43%. In its Argument-in-Chief, Union submitted that it had to compete for capital with other utilities across the United States and Canada and a 36% equity ratio puts Union at a disadvantage.[20]

In reply, Union submitted that none of the intervenors had challenged Union's position that other comparable utilities had higher equity ratios than 36% and that Union was lower relative to its peers. Union further submitted that no party challenged the comparability of Union to ATCO Gas or Terasen. Union disputed intervenors' argument that comparability has no value and noted that Dr. Booth, the expert consultant of the

[18] Oral Hearing Transcripts, EB-2011-0210, Volume 4 at p. 128 and Volume 5 at pp. 15 and 31.
[19] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at p. 105.
[20] Oral Hearing Transcripts, EB-2011-0210, Volume 13 at p. 53.

intervenors, in his testimony confirmed that the regulator should give weight to the deemed equity ratios of comparable utilities.[21]

CCC submitted that the Board consistent with its own policy must examine the individual circumstances of Union and in particular, the business and financial risk faced by Union to determine whether a change in capital structure is required. CCC further submitted that the use of comparators may supplement, but cannot replace that analysis. CCC also disputed Mr. Fetter's opinion that a higher equity ratio would allow Union to withstand future unforeseen events. CCC argued that Mr. Fetter's opinion was hypothetical.

Intervenors and Board staff submitted that Union had provided no evidence that it has not been able to compete for capital on favourable terms with other utilities. Intervenors and Board staff submitted that throughout the IRM period which coincided with a severe global financial crisis, Union had maintained a high credit rating. Union has been able to attract capital on reasonable terms under its current capital structure. Intervenors and Board staff referred to an interrogatory response[22] where Union confirmed that an equity ratio of 40% would not lead to a higher credit rating or a lower cost of debt. This view was also stated in the Standard and Poor's report which notes that Union would not get a higher rating than Spectra, its parent. In Reply, Union submitted that DBRS in its report noted that Union had requested a 40% deemed equity ratio. Union submitted that in that report DBRS expected Union to manage its balance sheet in line with the new regulatory capital structure and maintain greater financial flexibility commensurate with the current rating category. Union argued that this meant that Union would fit more appropriately with the current rating if it had a 40% common equity.[23]

Dr. Booth in his testimony expressed the view that one major aspect of risk was whether a utility was able to earn its allowed return on equity. Dr. Booth noted that since 2000, Union's average over-earning was about 2%. Intervenors and Board staff in their submission noted that Union had over-earned by approximately $278.7 million from 2007 to 2012. Intervenors and Board staff submitted that Union had provided no evidence to demonstrate a change in its risk profile. In reply, Union submitted that there

[21] Oral Hearing Transcripts, EB-2011-0210, Volume 6 at p. 61.
[22]Exhibit J.E-1-1-2.
[23] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at p. 102.

is a surplus of supply east of Union's Dawn to Parkway system and that posed a significant risk to Union. Union noted that there was further risk of turnback and this was reflected in lower revenues on Dawn to Kirkwall and M12.[24]

BOMA, in its submission, submitted that Union's interest coverage ratio was 2.74 which was higher than the 2% minimum interest coverage ratio set out in Union's trust indenture. This was higher than the ratios in 2008, 2009 and 2010 when it was 2.4%and 2.24% in 2007. However, the interest coverage ratio was lower than the threshold when the unregulated business was excluded from the calculation. BOMA further submitted that with respect to the interest coverage ratio, the common practice was to look at the entire company and not just the regulated portion of the business.[25] Union, in reply, disagreed with BOMA and submitted that this view was at odds with the general focus of intervenors that pursue to ensure that there is no cross-subsidy of the unregulated business by the regulated business. Union submitted that the intervenors wanted the Board to agree that it was appropriate to cross-subsidize the regulated business in order to meet the interest coverage ratio.

CCC in its argument cited the Ontario Court of Appeal in its decision (Toronto Hydro-Electric System Limited v. Ontario Energy Board, 2010) where the court stated that regulated utilities must balance the needs of shareholders and ratepayers. CCC submitted that if the proposed change in capital structure is approved, Union's shareholders will benefit by approximately $17 million while there would be no corresponding benefit within the test year to Union's ratepayers. CCC submitted that the Board should conclude that Union had not balanced the interests of its ratepayers and shareholders and accordingly disallow the change in the common equity ratio.

LPMA submitted that if the Board does approve Union's proposal or approves an equity ratio greater than the current 36%, then in that case, the Board would have to deal with how to treat preferred shares in the deemed capital structure. LPMA submitted that according to USGAAP, Union's preference shares were classified as equity by their auditors. LPMA submitted that there was no reason for the Board to deviate from the USGAAP treatment. SEC disagreed with LPMA and submitted that when the Board reviewed Union's capital structure in 2004, it did not consider preference shares to be equity and the Board should therefore refrain from doing so in this case. SEC submitted

[24] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at p. 107.
[25] Oral Hearing Transcripts, EB-2011-0210,Volume 14 at p. 88.

that the preference shares should be treated as long-term debt. Union agreed with SEC and noted that the Board had never considered Union's preference shares in any assessment of Union's common equity ratio. In addition, Union noted that they were not even considered relevant by Dr. Booth in his analysis.

SEC, in its submission, agreed with Union that the Board's Report on Cost of Capital is a guideline. However, it noted that the Board had thoroughly reviewed the business risk of Union in 2004 and unless there was a change in the business risk, there was no need for a utility to come before the Board with a different proposal. SEC submitted that Union was merely rearguing the 2004 case and there was no new evidence to show a change in risk.

SEC further submitted that Union had not articulated any benefits to ratepayers such as better access to market or lower borrowing costs, which Union already enjoys. In reply, Union submitted that the expectation that a higher equity ratio must be accompanied by lower borrowing costs or a ratings upgrade is unrealistic. Union therefore submitted that the Board should reject the submissions of intervenors.

Unlike other intervenors, LPMA and SEC submitted that Union's common equity ratio should be reduced from 36% to 35% consistent with what the Board had determined when it last reviewed the business risk and equity thickness of the company in 2004.

Cost of Debt

None of the intervenors raised any issues with the rates for short-term and long-term debt or preferred shares. LPMA however made a submission on the mix of short-term and long-term debt.

LPMA submitted that Union's proposal of a long-term debt ratio of 60.17% and a short-term debt ratio of -2.92% meant that ratepayers were being asked to pay a long-term debt rate on $108.5 million of borrowings and receive a credit at the short-term debt rate. LPMA submitted that this was not appropriate and was an indication that Union was over capitalized for rate base purposes.

LPMA noted that Union attributed the negative short-term debt to items outside of rate base that the utility has to invest in, such as construction work-in-progress and the contribution in excess of expenses for pension.

Union's average short-term borrowing for 2013 is predicted by LPMA to be $136 million[26] which represents approximately 3.66% of Union's rate base.

LPMA and SEC submitted that Union has more long-term debt than needed to finance rate base. This is under the scenario of a 36% and a 40% common equity ratio. At the same time, these scenarios have not included any short-term debt according to LPMA.

LPMA and SEC submitted that the Board should direct Union to include $136 million in short-term debt in the cost of capital calculation. Both parties further submitted that the balancing figure would be the long-term debt component. LPMA considered this to be an appropriate approach since in its view it was obvious that some of the long-term debt is being used to finance items outside of rate base.

In reply, Union noted that its cash position varied significantly due to the seasonal nature of its business. It further stated that long-term debt changes do not occur quickly and that the cash position would slowly return to short-term debt as the long-term debt level adjusted through maturities and reduced issues. Union submitted that issuing debt in small amounts was administratively burdensome and lumpy. Union indicated that it obtains long-term financing when prudent and tries to take advantage of favourable market conditions.

Union further submitted that having a negative short-term balance was not a new issue and the Board had addressed this before in the RP-2003-0063 proceeding. In the RP-2003-0063 Decision with Reasons dated March 18, 2004, the Board, on page112, determined that Union was in compliance with its deemed capital structure even though its long-term debt had marginally exceeded the 65% debt component of its approved capital structure. This excess was offset by a negative short-term debt balance.

Union emphasized that in the RP-2003-0063 Decision, the Board had used the word "marginal" to describe the level of excess in the long-term debt component. The actual

[26] Oral Hearing Transcripts, EB-2011-0210,Volume 5 at p. 40.

unfunded short-term debt was approximately $130 million in 2004 which is higher than the current unfunded short-term debt component of $115 million. Union submitted that the Board should reach a similar conclusion in this proceeding and not make any adjustments to the short-term or long-term debt component.

Board Findings

Deemed Common Equity Thickness

The Board finds that a deemed common equity ratio of 36% is appropriate for the 2013 test year, consistent with the deemed common equity ratio that was in place over the 2007 to 2012 period, inclusively.

The 2009 Cost of Capital Policy of the Board at page 43 sets out that for natural gas distributors such as Union, deemed capital structure is determined on a case-by-case basis and that reassessment of a gas utility's capital structure will only be undertaken in the event of significant changes in the company's business and/or financial risks.

Union filed no evidence in this proceeding that demonstrates its business and/or financial risks have changed over the period that the IRM Settlement Agreement was in place. In fact, Union stated many times during the proceeding that its business and financial risks have not changed and that it accepts that its overall risk profile has not materially changed since 2006.

Union put forth two arguments to support its application for a 40% deemed common equity ratio. The first is that the current deemed common equity ratio of 36% is too low and has never appropriately reflected its business and financial risk. Second, that the deemed common equity ratio should be increased solely on the basis of comparability; i.e., because other Canadian utilities now have higher deemed common equity ratios, the Board should also approve a higher deemed common equity ratio for Union.

The Board will address each of these two arguments in turn.

The Board does not accept the proposition that the deemed common equity thickness of 35% as determined by the Board in 2004 and subsequently increased to 36% as a result of a Settlement Agreement was incorrect and that it did not adequately reflect Union's financial and business risk profile. Union has filed no evidence to support this position that the deemed equity ratio was not correct and the Board therefore gives this argument little or no weight.

The Fair Return Standard (“FRS”) requires that a fair or reasonable return on capital should:

- Be comparable to the return available from the application of invested capital to other enterprises of like risk (the comparable investment standard);
- Enable the financial integrity of the regulated enterprise to be maintained (the financial integrity standard); and
- Permit incremental capital to be attracted to the enterprise on reasonable terms and conditions (the capital attraction standard).

Union’s second argument focuses on the first part of the comparable investment standard – that the return on invested capital must be comparable. However, Union’s argument fails to address the second part of the comparable investment standard, that being the issue of “enterprises of like risk”. Union would have the Board increase (and potentially reduce) its deemed common equity ratio in lock-step with the decisions of other regulators, without an analysis of whether the utilities to which it is compared are enterprises of like risk.

The Board acknowledges that there was a general consensus on the Canadian utilities that intervenors and Union asserted were comparable. The Board notes, however, that neither Union nor the intervenors filed analytical evidence that demonstrated that these utilities are of like risk to Union. Rather, what evidence was presented was anecdotal, ad hoc, and incomplete.

The Board is aware that since the 2008 financial crisis, the deemed common equity ratios of certain Canadian rate regulated entities have been increased. However, no evidence was filed in this proceeding that set out the risks that resulted in findings supporting higher deemed common equity for these utilities and no evidence was filed that demonstrates Union faces similar risks.

Union reiterated throughout the proceeding that its business and/or financial risks have not changed since 2006.

Accordingly, there is no reasonable basis for the Board to increase Union’s deemed common equity ratio above the 36% level presently reflected in rates.

The Board does not agree with the submission of SEC that a higher deemed equity ratio must be supported by benefits to ratepayers. The Board’s obligation to determine the

quantum of common equity (at issue in this proceeding) and the cost of that equity (subject to the Settlement Agreement) is governed by the FRS, which is a non-optional, legal standard.

The Board also does not agree with the submission of CCC that the Board must balance the interests of ratepayers and shareholders in determining the deemed common equity ratio. Consistent with the jurisprudence discussed in the 2009 Cost of Capital Policy, the Board remains of the view that it is not in the determination of the cost of capital that investor and consumer interests are balanced. This balance is achieved in the setting of rates.

Finally, the Board is of the view that there is no evidentiary basis to support a reduction in deemed common equity from the existing 36% to 35%.

Cost of Debt and Preferred Shares

The Board approves the cost of short-term, long-term debt, and preferred shares as per Appendix B, Schedule 3 of the Settlement Agreement. The Board notes that no issues were raised by intervenors or Board staff regarding the appropriateness of these costs during the proceeding.

Debt and Preferred Share Capitalization

The Board approves the amount of long-term debt, short-term debt, and preferred share equity as set out by Union in Exhibit J5.4, page 2, lines 7 through 12, which reflects the Settlement Agreement relating to this proceeding and deemed common equity of 36%.

The Board's findings on the amount of short-term and long-term debt are consistent with previous decisions of the Board and are consistent with Union's evidence that items outside of rate base are funded by short-term debt.

The Board has not undertaken a comprehensive review of whether it is appropriate for a gas utility to have preferred shares in its capital structure. The Board is generally aware that preferred shares are often referred to as "mezzanine capital", having characteristics of both debt and equity. There was no assessment of the characteristics of Union's issued and outstanding preferred shares in this proceeding. Similarly, there was no assessment of whether Union's issued and outstanding preferred shares should be considered to be common equity or debt for the purpose of determining Union's capital structure in order to set utility rates.

The Board will thus continue its current practice of approving the amount and cost of Union's preferred shares as a separate part of total utility capitalization. The Board notes, however, that the presence of preferred shares has the effect of reducing the amount of total debt capitalization in Union's capital structure.

COST ALLOCATION

General Cost Allocation Issues

Union provided a summary description of the methodology used to complete the cost allocation study, which supports the 2013 rate proposals. Union submitted that subject to the removal of the unregulated storage operations and certain proposals in Exhibit G1, Tab 1 (which are discussed below), the cost allocation study is consistent with the studies that were approved by the Board and used in the past, including in EB-2005-0520.

Union noted that the objective of the cost allocation study is to allocate the utility test year cost of service to customer rate classes for the purpose of acting as a guide to the rate design process. To allocate costs, the test year cost of service is analyzed to determine the appropriate functionalization and classification of costs. Union noted that the allocation of costs to individual rate classes is based upon these determinations.[27]

Union stated that the cost allocation study consists of three steps. These steps are:

Functionalization of costs to utility service functions: The first step of the cost allocation process is to associate asset and operating costs with the various utility service functions. There are four functions generally accepted as necessary to obtain and move gas to market: purchase and production of gas, storage, transmission, and distribution.

Classification of costs to cost incurrence (demand, commodity, customer): The second step categorizes functionalized asset and operating costs into classifications according to cost incurrence. The three main classifications are demand-related, commodity-related, and customer-related. Demand-related costs, also known as capacity-related costs are costs that vary with peak day usage of the system. Commodity-related costs are costs that are typically variable in nature and vary with the

[27] Exhibit G3, Tab 1, Schedule 1 at p. 1 (Updated).

level of gas consumed. Customer-related costs are costs that are incurred by virtue of a customer taking service and do not vary with either peak day demand or consumption.

Allocation of costs to rate classes: The final step in the cost allocation process attributes the three types of costs classified above. Allocation factors that reflect the underlying cause of cost incurrence are used in the allocation process. For example, demand-related costs are allocated using the peak day demands of each rate class. Commodity-related costs are allocated based on rate class consumption. Customer-related costs are allocated based on the number of customers in a rate class.[28]

Union noted that once these steps have been completed, costs allocated to each rate class can be totaled and compared to the revenue achieved.

Union noted that judgment is required in apportioning costs to the various functions and their sub-classifications. Union stated that this judgment is based on the specific knowledge of how its system is operated. As a result, a fully distributed cost of service study is used to provide an indication of cost responsibility by rate class at a specific point in time, but cannot and should not be viewed as a precise measurement of the actual cost to serve a particular rate class, much less a particular customer.[29]

Union noted that the cost allocation study for the current test year no longer includes costs associated with Union's unregulated storage business. Only utility costs relating to a maximum 100 PJ of storage space are included in the cost allocation study and used to allocate the cost of service to the utility rate classes.

Union noted that it allocated storage-related costs based on forecast in-franchise demand and system integrity requirements. All remaining storage-related costs, beyond the 100 PJ of regulated storage space, are allocated to the "Excess Utility Storage Space" category. Union charges its unregulated storage business the costs allocated to the Excess Utility Storage Space category for its use of the regulated storage space that is not required to meet in-franchise requirements. The total revenue requirement in this category, less compressor fuel, unaccounted-for-gas ("UFG") and non-utility system integrity costs, represents the cross charge to the non-utility. Accordingly, the allocators associated with regulated storage reflect only regulated activity.[30]

[28] Exhibit G1, Tab 1 at pp. 2-3 (Updated).
[29] Exhibit G3, Tab 1, Schedule 1 at p.2.
[30] Exhibit G1, Tab 1 at pp. 1-2. (Updated).

Union submitted that in conducting its analysis and preparing its cost allocation evidence, it used the Board's previously approved cost allocation methodologies, subject to the removal of the unregulated business and specific proposals which are discussed later in this Decision.

Board Findings

The Board generally accepts Union's cost allocation study and the resulting allocation of costs for the 2013 rate year. However, the Board has made findings on Union's specific cost allocation proposals below, which do impact, in some cases, the allocation of costs for certain groups of assets.

The Board notes that the allocation of costs, subject to the Board's findings on specific cost allocation proposals below, is approved only for 2013. The Board has some concerns with Union's 2014 rate redesign proposals (Rates 01 / 10 and Rates M1 / M2). Accordingly, the Board has directed Union, later in this Decision, to file an updated cost allocation study as part of its 2014 rates filing. The reasons associated with the Board's direction to file an updated cost allocation study are discussed in the section of this Decision that addresses Union's Rate 01 / 10 and Rate M1 / M2 rate redesign proposal.

System Integrity

Union noted that the 100 PJ of storage space reserved for in-franchise demands includes the space reserved for system integrity. System integrity space costs are included in the cost allocation study and allocated to utility rate classes and the Excess Utility Storage Space category. The Excess Utility Storage category includes the system integrity space costs for short-term storage and non-utility storage operations. Union submitted that it used the Board-approved methodology to allocate system integrity costs, except for its proposal related to storage pool hysteresis.

Consistent with the Board-approved methodology, Union proposed that the filled space costs continue to be allocated on the basis of storage space requirements. For purposes of determining storage pool hysteresis requirements, Union calculated a revised storage space requirement which includes total working storage capacity less non-utility third party storage space and system integrity space reserved for the Hagar LNG facility and storage hysteresis. Union noted that it requires empty system integrity space on November 1to manage late season injection demands. The space is

specifically held in reserve to manage the difference between in-franchise supplies and demands. Empty system integrity space is not required for short-term and long-term non-utility storage contracts as these contracts have little to no firm injection rights during October and November. Accordingly, Union proposed to allocate the empty system integrity space costs reserved for hysteresis based on the revised storage space excluding short-term and long-term non-utility storage space.[31]

The issue of system integrity space was partially settled as part of the settlement process. The Settlement Agreement states:

> For the purpose of settlement, the parties accept Union's proposed system integrity space value and its allocation for 2013. Acceptance is without prejudice to the examination at the hearing of matters pertaining to the actual use of utility storage space, including system integrity space, provided that the determination of this issue by the Board will not result in any change to the test year revenue requirement related to issues described under heading Exhibit B – Rate Base and heading Exhibit D – Cost of Service.[32]

Issue 6.4 is as follows: "Is the cost allocation study methodology to allocate the cost of system integrity appropriate?" The Settlement Agreement states that there is no settlement of this issue.[33]

Therefore, the issues relating to system integrity space that remain unsettled are whether the cost allocation study methodology for allocating the costs of system integrity space is appropriate and whether Union could use its fall integrity space as part of its winter integrity space.

No parties argued that the methodology used by Union to allocate the costs of system integrity space is not appropriate.

FRPO noted that Union has proposed that it would have two sets of contingency storage space - fall contingency space of 3.5 PJs and winter contingency space of 6 PJs. FRPO stated that the fall contingency space would be used in the event of a warmer than average weather and in providing extra space for continued storage

[31] Ibid at pp. 3-5.
[32] Updated Settlement Agreement, July 18, 2012 at pp. 15-16.
[33] Ibid at p. 19.

operations. The winter contingency space would be used to keep Union's storage operating during the critical periods of cold weather in the winter months.

FRPO postulated that the 3.5 PJs of fall contingency space could also be used as part of the 6 PJs of winter contingency space. Basically, FRPO asked Union to consider that if the 3.5 PJs of fall space were not filled, then that space could be subsequently used as part of the 6 PJs of space reserved for the winter. In that scenario, Union would make available an additional 3.5 PJs of storage space that could be used to sell short-term storage services (as it is now part of Union's Excess Utility Space classification). Union responded that it would be too expensive to fill that space in December and would result in a negative overall impact for ratepayers.[34]

FRPO argued that the price to fill that space is not necessarily more expensive in the winter (December fill) than for the fall (July fill).[35][36] As such, FRPO submitted that Union should consider using the 3.5 PJs of fall contingency space as a contributor to the 6 PJs of winter space. This would make available an additional 3.5 PJs of storage space and could provide a $3.0 million benefit to ratepayers as the storage contingency space would be better optimized.[37]

LPMA supported FRPO on this issue. LPMA submitted that the Board should direct Union to conduct an independent third-party analysis of the potential benefit of increased storage revenue (related to the availability of an additional 3.5 PJs of storage space) versus the potential cost additions for purchasing gas in the winter and selling that gas the following summer.[38] No other parties made submissions on this issue.

Union submitted that as no parties raised concerns regarding its methodology for allocating system integrity space, its proposal should be accepted by the Board.

With respect to FRPO's and LPMA's submissions on the use of its fall integrity space as part of its winter integrity space, Union submitted that there is considerable risk around this proposal and it is likely that any gas purchased after November would be at a higher cost. Union noted that it has never optimized its system integrity space. Union noted that the benefit that FRPO believes to be present is dependent on a number of

[34] Technical Conference Transcripts, EB-2011-0210, Volume 1 at pp. 73-75.
[35] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at pp. 144.
[36] Exhibit K14.5 at p. 32.
[37] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at p. 145.
[38] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p. 74.

factors which are out of Union's control, namely, fall weather, winter weather, summer / winter price differentials. Union submitted that what FRPO is proposing essentially amounts to gambling with the system integrity space. In Union's submission, as system operator, it is not prudent to do so.

In response to LPMA's suggestion that there could be a third-party study of the issue, Union submitted that there is no merit to that proposal as the outcome of the study would depend, in any particular year, on the summer / winter price differential and the fall weather / winter weather. For those reasons, Union submitted that FRPO's and LPMA's submissions should be rejected.[39]

Board Findings

The Board finds that Union's methodology for allocating system integrity space is appropriate. The Board notes that no parties raised concerns regarding this proposal.

The Board finds that the proposal made by FRPO and LPMA that the fall integrity space should be used as part of the winter integrity space is not adequately supported by the evidence in this proceeding. The Board notes that the increased revenue potential of $3.0 million cited by FRPO is hypothetical and in fact, the proposal could be detrimental to ratepayers depending on certain factors that are outside of Union's control (i.e. weather, price differentials, etc.). The Board notes that Union has stated that it has never optimized its system integrity space. The Board is of the view that the evidence in this proceeding does not support a change in approach.

The Board also rejects LPMA's suggestion that the Board direct Union to conduct an independent third-party analysis on this issue. The Board agrees with Union that the outcome of the study is likely to depend, in any particular year, on the summer / winter price differential and the fall weather / winter weather. Therefore, the results of the study may not be reliable for more than a year.

Tecumseh Metering Assets

Union noted that in its Board-approved 2007 cost allocation study, certain Tecumseh metering assets at the Dawn facility were reflected as transmission assets in its plant accounting records. These metering assets were directly assigned to the Dawn Station

[39] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at p. 135-136.

transmission function and the Dawn Station Customer classification. The costs were then allocated to the M12 rate class based on Tecumseh metering demands.

Union noted that based on a review of the Tecumseh metering assets, it updated the plant accounting records to move the assets from transmission to underground storage. However, as the Tecumseh metering assets continue to provide transmission service, Union directly assigned the Tecumseh metering assets to the Dawn Station transmission function. Similar to other underground storage assets functionalized to the Dawn Station, Union proposed to classify the costs to the demand classification and allocate the costs to rate classes based on the design day demand of Dawn compression. Union also proposed to eliminate the Dawn Station Customer classification, as the Tecumseh metering costs were the only costs previously allocated to this functional classification.[40]

LPMA supported this proposed change in the cost allocation methodology. LPMA noted that these assets provide transmission service to both ex-franchise and in-franchise customers, and the updated methodology is consistent with the allocation of costs of other interconnects in the Dawn Station. LPMA also stated that the impact of this proposal is not significant.[41]No other parties made submissions on this issue.

Union submitted that as no parties raised concerns with Union's proposal, it should be accepted by the Board.[42]

Board Findings

The Board approves Union's proposal as it relates to the Tecumseh Metering Assets. The Board finds that Union's updated cost allocation methodology for this group of assets is reasonable and is consistent with the allocation of other similar assets.

Oil Springs East Assets

Union proposed to change the functionalization, classification and allocation of costs associated with Oil Springs East assets for 2013. In Union's Board-approved 2007 cost allocation study, Union directly assigned the structure and improvements and

[40] Exhibit G1, Tab 1 at pp. 6-7.
[41] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 73.
[42] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 133.

measuring and regulating equipment plant costs associated with the Oil Springs East storage pool to the Dawn Trafalgar Easterly transmission function. This re-classification from underground storage to transmission was based on the use of the assets, which previously served Union North transmission needs. Union also classified the costs to the Dawn Trafalgar Easterly Oil Springs East Metering classification, and allocated costs to rate classes based on design day demand on the Dawn Parkway transmission system.

Union noted that its review of Oil Springs East storage pool assets determined that these assets now provide both storage and transmission services to customers. Accordingly, Union proposed to eliminate the direct assignment of Oil Springs East assets to the Dawn Trafalgar Easterly transmission function and functionalize these assets between storage and transmission. Union noted that this approach is consistent with the treatment of other underground storage assets at the Dawn facility that provide both storage and transmission services. Given Union's proposal to eliminate the direct assignment of Oil Springs East assets, Union also proposed to eliminate the transmission classification of Dawn Trafalgar Easterly Transmission for Oil Springs East metering.[43]

LPMA submitted that the changes to the allocation of the Oil Spring East Asset costs are appropriate. LPMA noted that Union's review has determined these assets provide both storage and transmission services to customers. As a result, Union proposed to functionalize these assets between storage and transmission, rather than continue the direct assignment of these assets to the Dawn-Trafalgar easterly transmission function.[44] No other parties commented on this issue.

Union submitted that as no parties have concerns with Union's proposal, it should be accepted by the Board.[45]

Board Findings

The Board approves Union's proposal as it relates to the Oil Springs East Assets. The Board finds that Union's updated allocation methodology for this group of assets is appropriate and notes that it is consistent with the treatment of other underground

[43] Exhibit G1, Tab 1 at pp. 7-8.
[44] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 72-73.
[45] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at p. 132.

storage assets at the Dawn facility that provide both storage and transmissions services.

New Ex-Franchise Services

Union noted that since Union's Board-approved 2007 cost allocation study was completed, several new ex-franchise transportation services have been developed by Union and approved by the Board. Specifically, Union has developed the C1 Dawn to Dawn-TCPL and C1 Dawn to Dawn-Vector firm transportation services, as well as the M12 firm all day (F24-T) transportation service.

Union proposed to include the costs associated with these new transportation services in its 2013 cost allocation study. A description of the cost allocation methodology proposed for each of the new transportation services is provided below.[46]

Dawn to Dawn-TCPL

Union noted that the C1 Dawn to Dawn-TCPL firm transportation service was developed to meet TCPL's need for a firm transportation service within the Dawn yard from Dawn to the Dawn-TCPL interconnect. Union's transmission system had the ability to accommodate requests for transportation on this path on an interruptible basis but required new facilities to offer the transportation service on a firm basis. This service was approved in EB-2010-0207.

Union noted that the costs of the Dawn to Dawn-TCPL firm transportation service include measuring and regulating assets, compressor fuel and UFG. Union proposed to directly assign the measuring and regulating gross plant, accumulated depreciation, and depreciation expense to the Dawn Station Demand classification and then to the C1 rate class. Similarly, the compressor fuel and UFG costs associated with the Dawn to Dawn-TCPL firm transportation service are also directly assigned to the C1 rate class.

Union stated that this cost allocation approach is designed to ensure that the costs associated with the provision of the Dawn to Dawn-TCPL firm transportation service are assigned to the C1 rate class and recovered in rates from customers utilizing the Dawn to Dawn-TCPL firm transportation service.[47]

[46] Exhibit G1, Tab 1 at p. 8.
[47] Ibid at p. 9.

No parties commented on this issue.

Dawn to Dawn-Vector

Union noted that the C1 Dawn to Dawn-Vector firm transportation service was developed to meet Greenfield Energy Centre LP's need for a firm transportation service within the Dawn yard from Dawn to the Dawn-Vector interconnect. This service was approved in EB-2007-0613.

Union noted that the costs of the Dawn to Dawn-Vector firm transportation service include the costs associated with compressor fuel and UFG. Consistent with Union's proposal for the Dawn to Dawn-TCPL transportation service, Union proposed to directly assign the compressor fuel and UFG costs to the C1 rate class.

Union stated that this cost allocation approach is designed to ensure that the costs associated with the provision of the Dawn to Dawn-Vector firm transportation service are assigned to the C1 rate class and recovered in rates from customers utilizing the Dawn to Dawn-Vector firm transportation service.[48]

No parties commented on this issue.

M12 Firm / All Day (F24-T)

Union noted that, as part of the NGEIR proceeding (EB-2005-0551), it developed an enhanced M12 F24-T transportation service that provides additional nomination windows and firm all day transportation capacity to power generators and other customers.

Union noted that the costs for the M12 F24-T transportation service include employee salaries and benefits and compressor maintenance costs. Union proposed to directly assign the employee salaries and benefits and compressor maintenance costs to the Dawn Trafalgar Easterly Transmission function and then to the M12 rate class.

Union stated that this cost allocation approach ensures that the costs associated with the provision of the M12 F24-T transportation service are assigned to the M12 rate

[48]Ibid at p. 10.

class and recovered in rates from customers utilizing the M12 F24-T transportation service.[49]

APPrO stated that it is opposed to Union’s M12 F24-T allocation methodology. APPrO argued that Union should include the cost of the additional nomination windows in the overall O&M cost of the Dawn-Trafalgar system, just as it does for the remainder of M12 capacity, where Union provides eight nomination windows for those shippers also contracting for TransCanada's STS service. APPrO argued that F24-T customers should not be paying a separate charge for extra nomination windows.

APPrO noted that F24-T is an add-on service to Union's M12 and C1 service. F24-T has nine additional nomination windows. F24-T is used by generators, as well as other customers that require additional nomination windows. The service is used in conjunction with non-utility storage so that these customers can access intra-day balancing services. Shippers using F24-T contract for TransCanada capacity downstream of Parkway.

APPrO noted that, under the Settlement Agreement, Union agreed to reduce the O&M budget by $0.5 million. Half of this amount is related to the reduction in provision for wages and salaries, and the other half is related to amounts attributable to non-utility services. APPrO stated that the net amount after these reductions is $0.65 million.

APPrO noted that Union provides a similar service for other M12 customers and for customers that contract for TransCanada's STS service. APPrO stated that STS and F24-T share the four standard NAESB nomination windows, as well as the four STS windows. As such, F24-T only has five incremental windows above the eight windows that are shared.

APPrO noted that Union does not charge STS customers a separate and distinct fee associated with providing the four extra STS nomination windows. APPrO noted that Union stated that it did not know if there were extra costs associated with providing these four extra nomination windows, but stated that if there are extra costs related to receiving and processing these nominations then these costs are embedded in the M12 rate, and not charged separately.

[49]Ibid at p. 11.

APPrO stated that F24-T shippers pay the same underlying M12 rate as a STS shipper which includes the cost for the eight nomination windows, and they also pay a separate charge for the extra nomination windows.

APPrO noted that Union has 1,250,000 GJs / day of M12 service that feeds into TransCanada's STS service. APPrO stated that this amount is significantly larger than the volume of F24-T shippers and has no extra nomination charge associated with it. APPrO proposed that the $0.65 million of annual O&M cost related to the F24-T service be included and recovered as part of the overall M12 costs and no specific charge apply to the F-24T customers.

APPrO submitted that this cost allocation would be done in the same manner as done for those M12 shippers contracting for STS service. To ensure that not all M12 shippers have access to the additional nomination windows, APPrO proposed that access be conditional upon the customer holding downstream FTSN capacity with TransCanada.

In the event that the Board determines that Union should charge a separate rate for F24-T, APPrO submitted that the costs allocated directly to F24-T should only reflect the increase in the five nomination windows (as opposed to the nine nomination windows as proposed by Union). This means that approx. $359,000 of the $645,000 would be allocated to F24-T, with the balance being recovered within the overall M12 service. In addition, APPrO submitted that Union should be required to use the billing determinants as shown in Exhibit J.G-9-13-1 of 442,154 GJs / day to calculate the F24-T charge.[50] No other parties commented on this issue.

Union stated that the premise of APPrO's argument is that Union accommodates STS windows within its overall O&M and does not separately charge for access to the STS windows as it does for F24-T. Union submitted that what APPrO's argument fails to recognize is that F24-T was specifically developed and agreed to as part of the NGEIR settlement to meet the needs of power generators.

The Settlement Agreement in the EB-2005-0551 proceeding speaks to this issue directly. Union noted that the Settlement Agreement states at page 14,

[50] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at pp. 139-142.

> "IT capital costs and the costs associated with the additional staffing required to implement F24-T, F24-S, UPBS and DPBS will be recovered from customers who elect the new services."

Union noted that the Settlement Agreement recognized that there would be incremental costs associated with providing F24-T service. As a result of the Settlement Agreement, F24-T service was added to the M12 rate schedule. Union argued that based on the above noted Settlement Agreement, the F24-T service should have a specific charge applied to reflect the incremental nomination windows available to those shippers.

In regard to APPrO's argument that the Board should direct Union to base the rate for the F24-T charge on the updated F24-T demands of 442,154 GJs / day, Union submitted that this change is immaterial and therefore it should not have to update the calculation for the charge.[51]

Board Findings

The Board approves Union's proposals as they relate to the Dawn to Dawn-TCPL service and the Dawn to Dawn-Vector service. The Board believes that these proposals adequately reflect cost allocation principles and are appropriate.

The Board accepts Union's M12 F24-T cost allocation methodology as filed, as it is consistent with the principle of cost causality.

Consistent with the Settlement Agreement in EB-2005-0551, the Board approves a supplemental service charge for F24-T customers. However, the Board agrees with the submission of APPrO that the charge should be calculated based on the costs associated with the 5 incremental nomination windows and be based on the updated F24-T demand, as set out in Exhibit J.G-9-13-1.

Other Cost Allocation Proposals

Union North Distribution Customer Stations Plant

Union currently allocates Union North customer station costs to its North in-franchise rate classes in proportion to average number of customers, excluding the small volume general service Rate 01 rate class. Union noted that the customer stations, however,

[51] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at pp. 141-143.

are constructed for customers that have hourly consumption in excess of 320 m^3. Assuming a typical industrial customer load factor of 40 percent and 20 hours of flow per day, the annual consumption for customers with a customer station would be a minimum of 934,400 m^3. Union noted that based on 2010 actual volumes, no Rate 01 customers and only a small percentage of Rate 10 customers consume 934,400 m^3 or more per year.

Union noted that all other medium and large volume customers require a total maximum daily requirement of 14,000 m^3 or more to be eligible for the respective firm contract rate classes (Rate 20 and Rate 100). Based on peak hourly flow equal to 1/20th of the maximum daily quantity of 14,000 m^3 or more, the approximate hourly consumption for the firm contract rate classes is 700 m^3. Accordingly, Rate 20 and Rate 100 customers exceed the hourly customer station requirement of 320 m^3.

Union proposed to allocate customer station costs based on the average number of customers, excluding the Rate 01 rate class and Rate 10 customers that do not meet the annual consumption threshold of 934,400 m^3.[52]

APPrO submitted that the change to the allocation of North Distribution Customer Station Plant is not appropriate. APPrO noted that Union's proposed change in allocation methodology has the effect of reallocating approximately $2.17M of revenue requirement from Rate 10 to Rates 20, 25 and 100.

APPrO noted that Union's proposed methodology is underpinned by the assumption that North customer station costs are only applicable to those customers that have an annual consumption greater than 934,400 m^3. APPrO submitted that the design criterion to size and install meters and regulators is the peak hourly load and pressure considerations. APPrO argued that annual consumption is not a design criterion. APPrO also noted that capital costs are driven by design criteria and not annual consumption.

APPrO submitted that Union's reallocation of North customer station plant costs is flawed because capital costs are dependent on the design criteria of peak hourly flow, not annual consumption. APPrO proposed that no change be made to the current allocation. In the alternative, to the extent that any changes are made, they should be consistent with the corrected Exhibit J.G-5-13-1, Attachment 1. Or in other words, on

[52] Exhibit G1, Tab 1 at pp. 12-13.

the average number of customers, excluding Rate 01 and the Rate 10 customers that do not meet the hourly consumption threshold of 320 m^3 / hour.

APPrO also noted that for those customers that take both firm and interruptible service, there is only one meter. Under Union's proposal, customers taking service under Rate 10, 20 or 100 are first allocated costs of the meter station for the firm load, and then they receive a second allocation of costs related to the customer station for the interruptible load. Therefore, APPrO submitted that there is a double allocation of costs caused by Union's proposal.[53] No other parties commented on this issue.

Union stated that APPrO advances two arguments in support of their position. The first is that the 934,000 m^3annual consumption figure is arbitrary, and the second is that because there may be overlap in the Rate 20 and Rate 100 with the Rate 25, the number of customers used in the allocation is overstated and results in double recovery.

As to the first argument, Union stated that the annual figure is not arbitrary. Union noted that 320 m^3/ hour, 20 hours a day, 365 days a year, aggregates to 934,400 m^3 / year.

As to the second argument, Union submitted that there is no double count of the allocation of costs. The costs of distribution customer stations are allocated and recovered from all contract rate classes, including interruptible classes, and customers taking a firm service in combination with an interruptible service pay for only a portion of the station costs in each of their rates. Union submitted that there is no over-recovery of North Distribution Customer Station Costs.[54]

Board Findings

The Board will not approve Union's proposal to reallocate the North Distribution Customer Station Costs. The Board agrees with the submissions of APPrO that since capital costs are dependent on the design criteria related to peak hourly flow, the reallocation of costs based on annual consumption is not appropriate.

The Board is of the view that since capital costs are dependent on the design criteria related to peak hourly flow, the allocation methodology should reflect the design criteria of peak hourly flow and not annual consumption. Therefore, the Board finds that the

[53] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 132-135.
[54] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at pp. 137-138.

North Distribution Customer Station Plant costs should be allocated on the basis ofthe average number of customers, excluding Rate 01 and the Rate 10 customers that do not meet the hourly consumption threshold of 320 m^3 / hour. The Board believes that this allocation methodology better reflects cost allocation principles. The Board directs Union to file this update as part of the Draft Rate Order process.

Distribution Maintenance – Meter and Regulator Repairs

Union noted that it currently classifies Union South distribution maintenance costs for meter and regulator repair to Distribution Customers and allocates the costs to the M2 rate class. For Union North, distribution maintenance costs for meter and regulator repair are classified to Distribution Demand and allocated to rate classes in proportion to the allocation of distribution meter and regulator gross plant.

Based on a review of its operating practices, Union determined that there are minimal maintenance costs associated with residential meters because it is more economical to replace small residential meters than perform repairs. To reflect Union's operating practices and harmonize cost allocation between Union North and Union South, Union proposed to align the Union North and Union South distribution maintenance meter and regulator repair cost methodology.

Union proposed to classify and allocate both Union North and Union South distribution maintenance costs for meter and regulator repair in proportion to the distribution meter and regulator gross plant cost allocation, excluding Rates M1 and 01.[55]

LPMA supported the proposal made by Union. LPMA agreed with Union that its proposal would harmonize the cost allocation between the North and the South and would better reflect its operating practices.

LPMA noted that Union's current M1 and Rate 01 rate classes include customers that have an annual consumption of up to 50,000 m^3 / year. Union proposed to change this effective January 1st, 2014 and reduce the number of customers in these classes by reducing the threshold to 5,000 m^3 / year. LPMA stated that it is not clear if Union's proposal would shift more costs associated with the maintenance costs from meter and regulator repairs into the M2 and Rate 10 classes as more customers are moved into those classes. LPMA stated that these additional customers will have their associated

[55] Exhibit G1, Tab 1 at pp. 13-14.

distribution meter and regulator gross plant costs moved with them, resulting in a greater proportion of the meter and regulator costs in these rate classes than the current split.

LPMA noted that at Union's next rebasing, where cost allocation will again be reviewed, the customers that use between 5,000 m^3/ year and 50,000 m^3 / year would now be in a class that attract the repair costs, even though Union's evidence in this proceeding is that the customers currently in Rates M1 and 01, which include these customers, would not attract repair costs. LPMA argued that this is most likely to be the case in the future, at least for the smaller volume customers that are proposed to be moved from Rates M1 and 01 to Rates M2 and 10, respectively. LPMA submitted that the Board should direct Union to address this potential issue in its next cost allocation study if the Board approves Union's proposal for the change in the split between the rate classes from 50,000 m^3 to 5,000 m^3.[56]No other parties commented on this issue.

Union submitted that no parties raised any concerns with the proposed allocation for 2013 and therefore the proposal should be approved by the Board. Union submitted that LPMA’s concerns related to the 2014 Rate M1 / M2 and Rate 01 / 10 rate redesign do not withstand any rigorous scrutiny and should be dismissed.[57]

Board Findings

The Board accepts Union’s proposal to classify and allocate both Union North and Union South distribution maintenance costs for meter and regulator repair in proportion to the distribution meter and regulator gross plant cost allocation, excluding the M1 and Rate 01 rate classes. The Board accepts Union’s submission that the harmonization of the cost allocation methodology between Union’s North and South operation areas better reflects Union’s operating practices and cost allocation principles.

Distribution Maintenance – Equipment on Customer Premises

Union currently allocates South distribution maintenance costs for equipment on customer premises to M1 and M2 customers based on service call time, and allocates North distribution maintenance costs for equipment on customer premises are allocated to rate classes based on a historic allocator.

[56] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at pp. 75-77.
[57] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at p. 139.

Union stated that the costs for maintenance of equipment on customer premises are primarily related to customer station maintenance. In order to more accurately reflect costs and to harmonize the allocation approach between Union North and Union South, Union proposed to allocate both the Union North and Union South Distribution Maintenance – Equipment on Customer Premises to rate classes in proportion to the allocation of customer station gross plant.[58]

LPMA supported Union's proposal regarding the allocation of Distribution Maintenance - Equipment on Customer Premises costs. LPMA submitted that Union's proposal would harmonize the approach in Union South and Union North, and more accurately reflect cost causation. LPMA also submitted this proposal is consistent with the proposal to allocate the distribution maintenance costs associated with the meter and regulator repairs.[59]

APPrO submitted that Union's proposal for allocating Distribution Maintenance - Equipment on Customer Premises costs is not appropriate. APPrO submitted that the effect of the proposal is to move $1.5 million in costs from Rate 01 to Rates 10, 20, 100 and 25. APPrO submitted that there is nothing on the record as to what the subject of this maintenance category is.

APPrO argued that the effect of the proposal in the South is to reallocate $0.32 million from the small volume rate class to larger volume rate classes. APPrO submitted that it has concerns with this proposal as these costs have been historically allocated to small volume customers, and now without regard for a full and complete understanding of the equipment involved, Union proposed to allocate these costs to the large volume rate classes. APPrO noted that the current methodology (in the North), as approved by the Board in EB-2005-0520, is to allocate costs in proportion to Appliance Rentals. APPrO stated that the reference to Appliance Rentals could be to equipment on customer premises, which have nothing to do with customer stations.

APPrO submitted that Union provided no evidence on what has changed between EB-2005-0520 and how that would result in this change in allocation methodology.

[58] Exhibit G1, Tab 1 at p. 14.
[59] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 77.

APPrO submitted that Union's proposal should be rejected in its entirety. APPrO submitted that a definition for customer station plant needs to be determined before an allocation methodology for these assets can be properly understood by parties and directed by the Board.[60] No other parties commented on this issue.

Union submitted that its proposal reflects the principle of cost causality harmonizes the North and South allocation methods and replaces the current Board-approved cost allocation methods that have outlived their purpose with a methodology that is up-to-date. As such, Union argued that its proposal should be accepted as filed.[61]

Board Findings

The Board will not approve Union's proposal to allocate both the Union North and Union South equipment on customer premises distribution maintenance costs to rate classes in proportion to the allocation of customer station gross plant. The Board agrees with the submission of APPrO that there is no evidence in this proceeding as to what the subject of this maintenance category is. Accordingly, the Board directs Union to file, in conjunction with the 2014 cost allocation study ordered elsewhere in this Decision, sufficient evidence to support this potential change in cost allocation, including a definition for this maintenance category and a delineation of what has changed since EB-2005-0520 that would result in a change to the allocation methodology.

Purchase Production General Plant

Union noted that it currently functionalizes general plant costs in proportion to the functionalization of rate base and O&M costs. However, general plant costs are functionalized to the Purchase Production function based on O&M costs only since there are no other plants costs functionalized to Purchase Production. The Purchase Production general plant costs are classified to Purchase Production Other and allocated to Union South in-franchise customers in proportion to delivery volumes, excluding the T1 and T3 rate classes.

Union proposed to classify general plant costs to both the Purchase Production System and Purchase Production Other classifications in proportion to the components of Purchase Production System and Other O&M. Union also proposed to allocate general plant costs to rate classes in proportion to the components of Purchase Production

[60] Oral Hearing Transcripts,EB-2011-0210, Volume 15 at pp. 135-139.
[61] Oral Hearing Transcripts,EB-2011-0210, Volume 16 at pp. 139-140.

System and Other O&M. Union noted that this methodology change ensures general plant costs that are functionalized to purchase production are classified and allocated to rate classes on the same basis.[62]

LPMA supported this proposal and no other parties commented on this issue.[63] Union submitted that no parties raised any concerns in regards to this proposal and therefore it should be approved as filed.[64]

Board Findings

The Board approves Union's proposal to update the allocation of purchase production general plant costs. The Board accepts Union's submission that this methodology better reflects cost allocation principles than the existing methodology.

Parkway Station Costs

Mr. Rosenkranz, an expert witness for CME, CCC, City of Kitchener and FRPO, described the manner in which the costs of transporting gas on the Dawn-Parkway transmission system are divided and allocated. Mr. Rosenkranz noted that these costs are divided into two distinct categories: the cost of the compressors needed to move gas from the Dawn Hub into the Dawn-Parkway system (Dawn Station costs); and all remaining costs (Dawn-Trafalgar Easterly costs). Mr. Rosenkranz noted that the Dawn-Trafalgar Easterly costs include Union's transmission pipelines, the compressors at Lobo, Bright, and Parkway, and the metering facilities at Kirkwall and Parkway. Dawn-Trafalgar Easterly costs are allocated using a distance-based commodity-kilometre methodology while Dawn Station costs are allocated on the basis of design-day demand.[65]

Mr. Rosenkranz noted that Union delivers and receives gas at Parkway and that the predominant direction of physical flow at Parkway is from Union to TCPL and Enbridge.[66][67] Mr. Rosenkranz noted that the metering and compression facilities at

[62] Exhibit G1, Tab 1 at pp. 14-15 (Updated).
[63] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 77.
[64] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at p. 140.
[65] Exhibit K10.7 at p. 2.
[66] Ibid at p. 3.
[67] Exhibit B1, Tab 9, Schedule 2 shows that the flows through Parkway are predominately export based.

Parkway Station are designed to meet Union's design day requirements to export gas from Union to TCPL and Enbridge.

Mr. Rosenkranz noted that metering costs are a function of design day demand and that compression horsepower at Parkway is determined by Union's peak day requirement to deliver gas to TCPL and Enbridge. In addition, Mr. Rosenkranz stated that Union's metering and compression assets at Parkway are not used to transport or deliver gas to any of Union's upstream in-franchise markets connected to the Dawn-Parkway transmission system. Therefore, Mr. Rosenkranz recommended that the Parkway station costs be separated from the overall Dawn-Trafalgar Easterly Transmission costs and allocated to rate classes on the basis of design day requirements.[68]

Mr. Rosenkranz noted that once the Parkway Station costs have been separated in the cost allocation, the costs should be recovered from those services that use the Parkway facilities. In addition, Mr. Rosenkranz recommended the establishment of a non-export M12 service that can be used by in-franchise customers to meet an obligated delivery requirement at Parkway. The non-export M12 service would allow shippers to deliver gas to Union but would not give shippers the right to deliver gas to TCPL or Enbridge. Mr. Rosenkranz recommended that the costs for this service should be allocated on the same basis as the Dawn-Trafalgar Easterly costs (exclusive of the Parkway Station Costs).[69]

Board staff[70], LPMA[71], BOMA[72], FRPO[73], Kitchener[74] and others supported the recommendations of Mr. Rosenkranz, as discussed above. LPMA submitted that the Parkway Station is not used to transport or deliver natural gas to any of the upstream in-franchise markets that are connected to the Dawn-Trafalgar transmission system. LPMA submitted that it is clear that the Parkway station metering and compression do not provide any benefits to in-franchise customers. As a result, these customers should not pay any of the associated costs.[75]

[68] Exhibit K10.7 at p. 3.
[69] Ibid at pp. 3-4.
[70] Board staff Argument, August 17, 2012, at pp. 19-20.
[71] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p. 77-82.
[72] BOMA Factum for Argument at p. 54.
[73] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at p. 158.
[74] City of Kitchener Argument, August 17, 2012, at p. 1.
[75] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p. 79.

Energy Probe supported Union's existing allocation of Parkway Station Costs[76]for four reasons. First, the peak design day criterion has not been challenged by parties. Second, if the proposal were to be accepted by the Board, more Parkway Station Costs would be borne by ex-franchise customers, exacerbating decontracting and lowering revenue which would need to be offset by higher rates to in-franchise customers. Third, costs would increase for customers of Enbridge. Finally, as per the Settlement Agreement relating to this application, the agreement to re-examine the Parkway delivery obligation could also result in changes to the treatment of the cost allocation for Parkway Station Costs.

Union noted that the treatment of Parkway station costs was last reviewed by the Board in EBRO 493/494. Union noted that with the exception of Energy Probe, which continues to support the current allocation, intervenors support Mr. Rosenkranz's proposal reflected in his evidence at Exhibit K10.7.

Union stated that the submission and recommendations of Mr. Rosenkranz are based on the premise that in-franchise customers receive little or no benefit from the Parkway Station and, therefore, in-franchise customers should not be responsible for Parkway Station costs. Union submitted that this premise is unfounded, and was determined to be so by the Board in EBRO 493/494. The Parkway Station provides benefits to in-franchise ratepayers in a number of ways. First, obligated deliveries received on the discharge side of Parkway provide a direct benefit to in-franchise shippers by reducing the size of the Dawn-Trafalgar facilities servicing in-franchise rate classes. Absent the Parkway obligation, in-franchise rates would be higher. Therefore, Union submitted that in-franchise ratepayers receive a substantial benefit from the existence of the Parkway Station.

Union also noted that its North in-franchise customers receive a benefit from being connected to Parkway because, without it, they could not access Dawn storage.

Union noted that in EBRO 486, it was directed by the Board to prepare an M12 cost allocation study to ensure that there was no cross-subsidiary among rate classes using the Dawn-Trafalgar transmission system. That study was filed with the Board in EBRO 493/494. The Board's decision addresses the allocation of the Dawn Station and Dawn-Trafalgar costs, including the Parkway Station.

[76] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at pp. 65-66.

Union submitted that nothing has changed as it relates to the design of the Dawn-Trafalgar system and the Parkway Station, and how it was used at the time of the EBRO 493/493 decision and how it is used now. On this basis, Union submitted that the proposal to change the allocation methodology should be rejected.[77]

Board Findings

The Board agrees with Union that in-franchise customers benefit from the Parkway Station. The Board also notes, as highlighted by Energy Probe, that there may be a number of unintended consequences associated with Mr. Rosenkranz's proposal, the consequences of which have not been considered in the context of this application. The Board will therefore not approve the separation of the Parkway Station costs from overall Dawn-Trafalgar Easterly Transmission costs, as proposed by Mr. Rosenkranz at this time. The Board will revisit this issue as part of Union's 2014 rates proceeding, after the Board receives Union's report on the outcome of the Parkway Obligation Working Group[78].

Kirkwall Station Costs

In its application, Union did not propose any changes to the allocation of the Kirkwall Station costs. LPMA noted that Mr. Rosenkranz also did not address the issue of Kirkwall metering costs in his evidence. LPMA submitted that the use of the Kirkwall Station has changed over the years and may change further in the future (given the changing flow of natural gas in the northeast area of North America which includes Ontario). LPMA stated these changing dynamics demonstrate the need to review the allocation of the Kirkwall Station costs. The changing flow of natural gas in the northeast has been highlighted by Union in this proceeding through the level of turn-back of M12 capacity that has already occurred and is forecast to occur in the future.

LPMA noted that the Parkway-to-Maple bottleneck has been raised in this proceeding. The dramatic increase in TCPL tolls, especially along the northern Ontario route relative to other routes to the Greater Toronto Area, has illustrated the potential need for the Parkway West project. LPMA stated that all of these issues highlight the fact that there has been considerable change that has taken place with respect to the flows of gas around the Parkway Station, since Union last reviewed the cost allocation and rate

[77] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at pp. 143-145.
[78] Union Settlement Agreement, June 28, 2012, Section 3.17, p.16

design for services offered on the Dawn-Trafalgar system in 1995, and that the Board last approved in Union's 1997 rate case, which was EBRO 493/494. LMPA submitted that the Board should direct Union to review the allocation of Kirkwall metering costs.[79] No other parties commented on this issue and Union did not respond to LPMA's submission in reply.

Board Findings

The Board agrees with the submissions of LPMA. The use of the Kirkwall Station has changed substantially over the years and there is a clear need to review the allocation of Kirkwall Station costs. The Board directs Union to undertake a review of the allocation of Kirkwall metering costs as part of its updated cost allocation study which the Board has directed Union, later in this Decision, to file in its 2014 rates filing.

Dawn-Trafalgar Easterly Costs

Union's Dawn-Trafalgar Easterly costs include Union's transmission pipelines, the compressors at Lobo, Bright, and Parkway, and the metering facilities at Kirkwall and Parkway. Dawn-Trafalgar Easterly costs are allocated using a distance-based commodity-kilometre methodology.

LPMA submitted that, with the removal of the Parkway station metering and compression costs discussed above and subject to the review of the Kirkwall metering costs also noted above, the allocation of the remaining Dawn-Trafalgar Easterly costs should continue to be based on the distance-based commodity-kilometre methodology. LPMA argued that there has been no evidence presented in this proceeding to suggest that this allocation methodology is not appropriate for these remaining costs, nor has any evidence been presented in support of another methodology.[80] No other parties commented on this issue.

Board Findings

The Board approves Union's proposed allocation of the Dawn-Trafalgar Easterly costs. The Board finds that the distance-based commodity-kilometre methodology used to

[79] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 80.
[80] Ibid. at p. 81.

allocate the Dawn-Trafalgar Easterly costs is appropriate and reflective of cost allocation principles.

Utility / Non-Utility Storage Cost Allocation

Board staff noted that Union's methodology for separating its utility and non-utility storage businesses was originally approved by the Board in EB-2005-0551 and confirmed by the Board in EB-2011-0038. In the EB-2011-0038 Decision and Order, the Board stated:

> The Board finds that the intent of the NGEIR Decision was to effect the one-time separation of plant assets between Union's utility and non-utility businesses. Therefore, there is no need for a subsequent separation (or the filing of another cost study).[81]
>
> The Board finds that Union has appropriately applied its 2007 Cost Allocation Study for the one-time separation of plant.[82]

Union, in this proceeding, provided a description of its methodology for allocating costs related to storage additions. Union provided the following table:

Description	Allocation Methodology
New Storage Asset – increase in capacity or deliverability	100% Allocation to unregulated
New Storage Asset – no increase in capacity or deliverability	Allocated regulated versus unregulated based on the historic allocation of assets at that location
Replacement Asset – no increase in capacity or deliverability	Allocated regulated versus unregulated based on the historic allocation of assets being replaced.
Replacement Asset – increase in capacity or deliverability	Cost of replacing the existing asset like for like is allocated regulated versus unregulated based on the historic allocation of assets being replaced. The cost of providing the incremental capacity or deliverability is allocated 100% to the unregulated operation. This results in a new blended rate for this asset.

With respect to the allocation of O&M costs related to non-utility storage, Union stated that:

[81] Decision and Order, EB-2011-0038,January 20, 2012 at pp. 6-7.
[82] Decision and Order, EB-2011-0038,January 20, 2012 at p. 11.

a) Actual O&M related to the operation of the storage facilities was allocated to the non-utility storage operation using the same allocators applied to the assets for that facility.

b) Administrative and general expenses and benefits in support of non-utility storage operations were allocated in proportion to storage O&M.

c) O&M costs related to the development of new storage assets are assigned based on an estimate of time spent annually on the development of non-utility projects.

d) O&M costs related to the Regulatory Department for development of new storage assets, are assigned based on an estimate of time spent annually on the development of non-utility projects.[83]

Board staff supported the methodologies for allocating capital and O&M costs to non-utility storage as described above.

Board staff also noted that as a result of Union's review of its allocation factors in early 2012[84], which sought to confirm that the methodology set out above was applied correctly, Union identified updates that were required to10 of its storage pools. Union noted that after the allocation factors were updated, it compared the updates against its 2013 rate evidence. Union determined that the use of the revised allocation factors for storage capital additions would have decreased the utility storage assets by approximately $25,000 in 2013. Union also noted that the allocation factor update results in a decrease to utility O&M of $100,000.[85]

Board staff submitted that although these amounts are quite small, the Board should require Union to update its allocation factors as part of its evidence in this proceeding and reassign the noted amounts from utility to non-utility ($100,000 in O&M and the revenue requirement related to the $25,000 in decreased utility storage capital costs).

Board staff also submitted that the above noted methodology for allocating costs between utility and non-utility storage related to storage additions should continue going

[83] Exhibit A2, Tab 2, p.8.
[84] This review occurred as a result of recommendations in the Black & Veatch report filed in EB-2011-0038.
[85] Union - Supplemental Question Responses, FRPO Supplemental Question #2.

forward and that the allocation of utility / non-utility storage costs should be updated in every rebasing and be reflected in the pre-filed evidence. [86] BOMA supported Board staff's submission on this issue.[87]

FRPO submitted that Union has under-allocated storage plant additions to the non-utility storage operation by continuing to use the same plant allocation factors that were developed for the one-time separation of plant. FRPO noted that Union refers to these as original or historic allocation factors. FRPO submitted that Union needs to update these factors each year to reflect the changes in the relative amounts of utility and non-utility storage. FRPO noted that Union provided updated allocation factor for each storage asset. FRPO noted that Union has stated that if it had used the revised updated factors to allocate plant additions for maintenance capital projects, the estimated allocation of plant to non-utility storage would have been $50,000 higher in 2012 and $25,000 higher in 2013. FRPO noted that, however, Union did not provide actual information for the years 2007 through 2011, even though the impact of Union's failure to update the cost allocation factor on 2013 rates depends on the cumulative misallocation of plant additions since 2007, not just the allocations during the bridge year. FRPO noted that Union does not propose to make any adjustment in 2013 to correct this error. FRPO argued that the allocation of plant to non-utility storage should be increased by $25,000 for 2013 and that Union should provide evidence (continuity schedules) supporting this allocation change prior to its 2014 rates proceeding.

FRPO noted that Union's failure to update the plant allocation factors also means that O&M was under-allocated to non-utility storage operation for 2013. FRPO noted that according to Union, the utility O&M costs should be reduced by approximately $100,000 based on its update to storage allocation factors. FRPO submitted that the 2013 utility O&M amount should be reduced by $100,000 and that the O&M amount for non-utility storage should be updated annually.

FRPO also raised a concern regarding the allocation of general plant to non-utility storage. FRPO submitted that Union has under-allocated general plant additions to non-utility storage plant by failing to update the other general plant allocation factor.

FRPO noted that the one-time separation of storage plant included an allocation of general plant. Two separate allocation factors were used, one factor for vehicles and a

[86] Board Staff Submission, August 17, 2012, at pp. 21-24.
[87] BOMA Factum for Argument at p. 54.

second factor for general plant. FRPO noted that the other general plant allocation factor that was used for the one-time separation was 2.92%. FRPO noted that this factor is the arithmetic average of the ratio of non-utility storage plant to total plant, 3.2%, and the share of non-utility support costs in the total O&M, which at the time of separation was 2.52%. FRPO stated that Union has not updated the other plant allocation since the one-time separation of plant.

Based on plant and O&M shares for year-end 2010, FRPO estimated the other plant allocation factor should be raised from 2.92% to at least 4%. Using the 4% other plant allocation factor, FRPO estimated the under-allocation to Union's non-utility storage business related to the allocation of general plant costs.[88]

FRPO noted that the application of the 4% other plant allocation factor across 2010, 2011, 2012 and 2013 shows an increasing under-allocation of non-utility, which peaks at $306,000 for 2013. FRPO requested that Union be directed to make the changes to the other general plant allocation factor using the most up-to-date information available prior to the implementation of 2013 rates.[89]

FPRO also requested that the Board direct Union to file plant continuity schedules related to Union's non-utility business as part of its 2014 rates filing.[90] FRPO and Energy Probe also submitted that the Board should direct Union to have Black and Veatch update the report that was filed in EB-2011-0038 as part of its 2014 rates filing.[91]

Union submitted that the updates to the storage related O&M and capital costs that parties are suggesting be made are immaterial. Union stated that the total amount of this update is approx. $50,000. In Union's submission, the quantum of the change does not warrant the treatment that parties are proposing. Union stated that it has a robust methodology to manage plant additions and plant replacements.

Union also submitted that there is no reason for Black & Veatch to revisit this issue again. It was first considered in the EB-2010-0039 case, and again in EB-2011-0038 and the report contains up-to-date information.[92]

[88] FRPO Argument Compendium at p. 22.
[89] Oral Hearing Transcripts, EB-2011-0210,Volume 14 at pp. 134-142.
[90] Oral Hearing Transcripts, EB-2011-0210,Volume 14 at p. 140.
[91] Oral Hearing Transcripts, EB-2011-0210,Volume 14 at pp. 63-64.
[92] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at pp. 146-147.

Board Findings

The Board finds that Union's allocation methodologies for capital additions and O&M costs related to its utility and non-utility storage operations are appropriate. The Board is of the view that these allocation methodologies reasonably reflect cost allocation principles.

The Board notes that, based on a review that Union undertook in early 2012 regarding its utility and non-utility storage allocations, Union identified certain allocation factor updates that are required to a number of its storage pools. The Board directs Union to implement the storage allocation factor update as part of this proceeding. The Board notes that there seems to be a misunderstanding among parties as to the dollar amount that is the outcome of the allocation factor update. The Board notes that Board staff stated that the allocation factor update results in an approximate decrease in utility storage assets of $25,000 and a decrease in utility O&M of $100,000 for 2013. However, Union stated that the total amount related to this update is $50,000. The Board directs Union to explain which amount is the correct amount that needs to be updated to reflect the change in allocation factors. The Board directs Union to implement this change as part of the Draft Rate Order process.

With respect to FRPO's argument that an update is also required to the general plant allocation, the Board finds that it does not have sufficient evidence on this issue to make this finding. While the Board is of the view that there may or may not be an under-allocation of general plant to Union's non-utility storage operation, the quantum of that under-allocation, if any, is not clear from the evidence in this proceeding. Therefore, the Board will not direct Union to make an update to the general plant allocation for the purpose of setting 2013 rates.

However, the Board finds that in order for parties, and the Board, to confirm that the allocation of storage costs between Union's utility and non-utility storage operations is correct, the Board requires up-to-date continuity schedules related to Union's non-utility storage business. The Board directs Union to file, as part of its 2014 rates filing, these continuity schedules.

Also, the Board directs Union to hire an independent consultant to update the report that was filed in the EB-2011-0038 proceeding and file that report as part of its 2014 rates proceeding.

The Board believes that it should have a robust evidentiary record in Union's 2014 rates proceeding on all issues related to the allocation of storage costs between utility and non-utility storage. The Board notes that, as part of Union's 2014 rates filing, it will revisit the allocation of all storage related costs between Union's utility and non-utility storage operations. At that time, the Board may also order further updates to the allocation factors (including the general plant allocation factor).

RATE DESIGN

General Rate Design Issues

Union noted that when designing its 2013 proposed rates for Union North and Union South, the following factors were taken into consideration:

- The revenue deficiency for the company as a whole;
- The relative rate changes of other rate classes;
- The allocated cost of service;
- The level of current rates and the magnitude of the proposed change;
- The potential impact on customers;
- The level of contribution to fixed cost recovery;
- Customer expectations with respect to rate stability and predictability; and
- Equivalency of comparable service options.

Union stated that the revenue-to-cost ratios reflect Union's application of accepted rate design principles and are underpinned by the cost allocation study. Union also submitted that the 2013 proposed revenue-to-cost ratios are within an acceptable range and are generally consistent with those approved by the Board in EB-2005-0520.[93]

In an interrogatory response, Union noted that revenue-to-cost ratios are the outcome, not an input, of the application of Union's rate design considerations described above. Union submitted that acceptable revenue-to-cost ratios must:

[93] Exhibit H1, Tab 1, p. 12 (Updated).

- Satisfy rate design principles discussed above, and
- Bear a reasonable relationship to previously approved revenue-to-cost ratios.

Union stated that acceptable revenue-to-cost ratios guidelines include:

1. Firm in-franchise general services (Rate 01, Rate 10, Rate M1 & Rate M2) close to unity.
2. Large firm in-franchise contract services (Rate T1, Rate T3 and Rate 100) close to unity.
3. Other in-franchise firm services between (1) and (2) above will vary due to firm rate continuum considerations. A revenue-to-cost ratio approximating 80% or more is generally realized.
4. Rate M12 firm transportation service close to unity.
5. Interruptible in-franchise service pricing is set in relative relationship to firm services, with the resulting revenue-to-cost ratios showing greater deviation from unity.[94]

Board staff submitted that Union's rate design considerations (and revenue-to-cost ratio guidelines), discussed above, are appropriate. However, Board staff raised a number of concerns regarding how these rate design considerations were followed.

Board staff stated that a general principle is that approved revenue-to-cost ratios, for in-franchise customers, should not move away from a unity position. In a number of in-franchise rate classes, the EB-2005-0520 Board-approved revenue-to-cost ratios were closer to unity than proposed in this case. These rate classes are: Rate 01 (from 0.976 to 0.975), Rate 25 (from 0.467 to 0.446), Rate M2 (from 0.972 to 0.940), Rate M5A (from 0.824 to 0.746), and Rate M10 (from 0.131 to 0.073).[95]

Union provided the following rationale for these changes. Union stated that the proposed rate is designed to manage the relationship between the firm and interruptible service, maintain the rate continuum across all of the firm rate classes and the interruptible rate class, and to manage the level of rate increases to the rate classes.[96] Board staff noted that these may be reasonable reasons to breach the general principle

[94] Ex. J.H-1-5-2.
[95] Ibid.
[96] Oral Hearing Transcripts, EB-2011-0210, Volume 12 at p. 8.

of not moving away from unity.

In response to Union's proposal to increase rates in Rate M1 to slightly beyond unity (1.003) and over-recover from that rate class by an amount of $1.14 million, Board staff submitted that this over-recovery (which results in cross-subsidization) is not appropriate.[97] Rate M1 (Union's small volume general service class in the South) should not have to pay more costs than are allocated to that class (on the basis of the cost allocation study). Board staff noted that Rate M1 is Union's only in-franchise rate class with a revenue-to-cost ratio higher than 1.0. Board staff noted that Union is attempting to balance the rate continuum and help offset larger rate increases in other rate classes by over-recovering in Rate M1. In Board staff's view this proposal is unfair to Union's M1 customers. Board staff submitted that Rate M1's rate design should not result in a revenue-to-cost ratio higher than 1.0.

Board staff noted that Union is materially under-recovering from Rate M7 ($1.2 million) and Rate M12 ($2.6 million) and that these rate classes have delivery rate impacts of less than 2%.[98] Board staff noted that for rate continuum purposes further rate increases for Rate M7 are not feasible. However, Board staff stated that Rate M12 does not have the same rate continuum constraints as does M7. Board staff submitted that Union should increase its rates in Rate M12 to result in a revenue-to-cost ratio of 1.0.

Board staff also commented on Union's allocation of S&T margins to the rate classes. Board staff noted that the overall revenue deficiency (after the proposed rate increases have been applied) for Union's Northern in-franchise rate classes is $13.125 million and the overall revenue deficiency (after the proposed rate increases have been applied) for Union's Southern in-franchise rate classes is $10.778 million. The overall revenue deficiency for in-franchise rate classes (after the proposed rate increases have been applied) is $23.903 million.[99] These amounts are offset by the S&T margins of $23.903 million that are built into rates. Board staff noted that approximately 55% of S&T margins are being allocated to the North and approximately45% are being allocated to the South. Union noted that the methodology for the split in the S&T margin allocation between operation areas is that the same proportion of the total revenue deficiency (before proposed revenue increases are applied) should be recovered by S&T margin allocations in both operation areas.[100] This methodology results in approximately 30%

[97] Exhibit H3, Tab 1, Schedule 1.
[98] Ibid.
[99] Ibid.
[100] Oral Hearing Transcripts, EB-2011-0210,Volume 11 at pp.146-148.

of the total revenue deficiency in each operation area being recovered through the allocation of S&T margins.[101]

Board staff submitted that although the methodology used by Union as discussed above results in an equitable allocation of S&T margins between operating areas (from the perspective of offsetting the revenue deficiency) it has no correlation to the manner in which the revenues are derived and is different from the last allocation of S&T margins in 2007 (EB-2005-0520).

Board staff noted that Union has acknowledged that it is using the S&T margins as a rate design tool to manage rate impacts, rate continuity and revenue-to-cost ratios in 2013.[102] In its Argument-in-Chief, Union submitted that using these margins as a rate design tool has been done in the past and is appropriate.[103]

Board staff noted that the Board, in this proceeding, needs to determine whether the allocation of S&T margins should be properly considered a rate design tool. Board staff is of the view that the allocation of S&T margins should not be used as a rate design tool. Board staff submitted that there are more appropriate ways to allocate these revenues which have more direct linkages to the manner in which the S&T margins are generated. BOMA supported the submissions of Board staff.[104]

LPMA supported Board staff's submissions that the M1 revenue-to-cost ratio should be no higher than 1.0 and that the M12 revenue-to-cost ratio should be increased to 1.0.[105]

VECC supported Board staff's submission that the M1 revenue-to-cost ratio should be no higher than 1.0. VECC also submitted that it has some concerns regarding Union's allocation of S&T margins. VECC stated that Union has allocated the S&T margins to rate classes for the purpose of managing rate impacts, with no regard for the causal connection between the generation of S&T revenues and the classes that pay for the assets that generate the S&T revenues. VECC stated that allocation of these revenues should be based on some equitable distribution across all distribution ratepayers.[106]

[101] Exhibit H3, Tab 1, Schedule 1.
[102] Oral Hearing Transcripts, EB-2011-0210, Volume 12 at pp. 121-122.
[103] Oral Hearing Transcripts, EB-2011-0210, Volume 13 at p.81.
[104] BOMA Factum for Argument at p. 54.
[105]Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p.89.
[106] VECC Argument, August 21, 2012 at p. 24-25.

Union submitted that the revenue-to-cost ratios are reasonable as filed. Union noted that the revenue-to-cost ratios are the outcome of the rate design process and reflect the application of the rate design principles described in Exhibit H1, Tab 1 (and cited above). Union noted that there has never been a requirement that revenue-to-cost ratios be limited to 1.0. Union noted that, in 2007, the Board approved rates for Rate 10 that resulted in a revenue-to-cost ratio of 1.058.

Union submitted that the principal submission made by most intervenors on this topic is that the revenue-to-cost ratio for Rate M1 should be adjusted from the proposed level of 1.003 down to 1.0. A number of parties have suggested that this adjustment could be funded by increasing the M12 revenue-to-cost ratio from 0.984 to unity. Union submitted that the revenue-to-cost ratio of 1.003 is not materially different from 1.0 and is not inconsistent with resulting revenue-to-cost ratios approved by the Board in the past.

With respect to M12, Union submitted that the revenue-to-cost ratio of 0.984 is consistent with the cost-based Board-approved rate design for M12 services. Union noted that the M12 revenue-to-cost ratio is less than 1.0 because Dawn-Trafalgar westerly service revenues earned under C1 rate schedule reduce M12 rates. Increasing the M12 revenue-to-cost ratio to 1.0 would result in over-recovery of Dawn-Parkway costs presently allocated to ex-franchise services.

Union also made submissions on the issue raised by Board staff and VECC on the use of S&T margins as a rate-making tool. Union stated that it does not agree with the position of Board staff and VECC. Union noted that the use of S&T margin for rate design purposes has been a long standing and necessary feature of Union's rate design process. Absent the ability to use S&T margin for rate design, Union would need to deal with rate impacts and rate continuity issues by adjusting revenue-to-cost ratios alone. As part of the rate design process, Union has allocated approximately $13.1 million of S&T margins to the North and approximately $10.8 million of the S&T margins to the South. Union stated that this is a greater proportion than has ever been allocated to the North. Union noted that it is seeking to recover proportionally the same level of revenue deficiency between Union North and South because it reasonably balances the need to manage rate impacts in the North and the need to address rate continuum concerns in the South. Union submitted that using S&T margin to smooth rate continuum impacts and to manage rate design considerations is a longstanding feature of Union's rate design, and it should be continued by the Board in this proceeding.

Board Findings

The Board finds that Union's rate design considerations and revenue-to-cost ratio guidelines are generally appropriate. However, the Board has concerns with some of Union's rate design proposals, as discussed below.

The Board agrees with Board staff, that in general, applied-for revenue-to-cost ratios for in-franchise customers should not move farther away from 1.0 than the revenue-to-cost ratios that are presently approved and reflected in rates. The Board notes that for a number of in-franchise rate classes, the EB-2005-0520 Board-approved revenue-to-cost ratios were closer to unity than the revenue-to-cost ratios proposed in this proceeding. These rate classes are: Rate 01 (from 0.976 to 0.975), Rate 25 (from 0.467 to 0.446), Rate M2 (from 0.972 to 0.940), Rate M5A (from 0.824 to 0.746), and Rate M10 (from 0.131 to 0.073). As a result, the Board finds that the proposed revenue to cost ratios are not appropriate.

The Board notes that some parties made the argument that the revenue-to-cost ratio should be no greater than 1.0 for the M1 rate class. The Board agrees with this submission and is of the view that no compelling rationale was provided by Union to support a revenue-to-cost ratio for the M1 rate class greater than 1.0. Therefore, the Board finds no in-franchise rate class should have a revenue-to-cost ratio greater than 1.0.

The Board finds that Union's use of the S&T margins as a rate design tool to manage rate impacts, rate continuity and revenue-to-cost ratios in 2013 is not appropriate. The Board believes that S&T margins should be allocated to rate classes on the basis of sound regulatory principles. The Board does not agree that these margins should be used arbitrarily to manage rate impacts.

The Board notes that elsewhere in this Decision, the Board has found that certain optimization activities are to be considered part of gas supply, removing these activities from what Union has previously defined as transactional services and included in its S&T margin forecast. In this Decision, the Board has defined optimization as any market-based opportunity to extract value from the upstream supply portfolio held by Union to serve in-franchise bundled customers, including, but not limited to, all FT-RAM activities and exchanges. The net revenues related to these optimization activities are no longer to be included in the S&T margin forecast.

The Board finds that optimization related net revenues should be allocated to those customers that pay the costs of facilitating Union's gas supply plan. Therefore, the Board directs Union to file a proposed allocation methodology, as part of the Draft Rate Order process, which allocates the optimization margins to those customers. The Board notes that this proposal must be based on regulatory principles.

With respect to the remaining S&T margins, the Board notes that this Decision sets out sub-categories for these margins including: Long-Term Transportation related S&T margins, Short-Term Transportation related S&T margins, and Storage and Other Balancing Services related S&T margins. The Board directs Union to file allocation methodologies for the above noted sub-categories, as part of the Draft Rate Order process, which reflect regulatory principles.

The Board directs Union to use its proposed methodologies to allocate the S&T margins to its rate classes as part of the Draft Rate Order process. The Board also notes that the methodologies for allocating S&T margins that are ultimately accepted by the Board are to be used in Union's next rates proceeding (cost of service or IRM).

The Board expects, as part of the Draft Rate Order process, that Union will file revised rates that reflect all of the findings in this Decision and that reflect the rate design principles ordered by the Board above.

Rate 01 / 10 and Rate M1 / M2 – Volume Breakpoint and Rate Block Harmonization Proposal for 2014

Union proposed to lower the annual volume breakpoint between the Rate 01 and Rate 10 rate classes in Union North and the Rate M1 and Rate M2 rate classes in Union South from 50,000 m^3 to 5,000 m^3. Union also proposed to harmonize the rate block structures in the small volume general service rate classes (Rate 01 and Rate M1) and in the large volume general service rate classes (Rate 10 and Rate M2). Union proposed to utilize the current Board-approved rate block structures for Rate M1 and Rate M2 in Union South for Rate 01 and Rate 10 in Union North respectively. Union proposed to implement the annual volume breakpoint and rate block structure changes on a revenue neutral basis effective January 1, 2014.[107]

[107] Exhibit H1, Tab 1 at p. 14 (Updated).

Union noted that its proposal to lower the annual volume breakpoint between small volume general service rate classes (Rate 01 and Rate M1) and large volume general service rate classes (Rate 10 and Rate M2) to 5,000 m^3 from 50,000 m^3 will improve the rate class composition of Rate 01 and M1 and achieve more homogeneous rate classes. Also, Union noted that the proposal will improve the rate class size in Rate 10 and Rate M2, which will ensure viable large volume general service rate classes and improve rate stability.[108]

All parties agreed with Union's proposition that the volume breakpoint between the Rate 01 / Rate 10 and Rate M1 / M2 should be reduced for the reasons cited above and that the rate blocking structure should be harmonized. However, no party agreed with the methodology used by Union to give effect to its proposal. Board staff[109], LPMA[110], SEC[111] and other parties explicitly raised concerns regarding Union's methodology for allocating costs between the noted rate classes.

LPMA noted that with respect to the customer-related costs, Union has used a customer-weighting factor to determine the amount of customer-related costs that are associated with the customers that will be moving rate classes. LPMA noted that the weights used are 1.0 for residential, 1.5 for commercial, and 2.0 for industrial. LPMA noted that when asked if Union had any empirical evidence to support the relative differences in the weights used, Union replied that the empirical evidence that they have in this is similar to the evidence that they used when they did the 2007 rate split, which used the same weightings. LPMA noted that Union filed a report in support of the 2007 split prepared by Navigant Consulting Inc. that simply stated that the weights currently used by Union were 1.0 for residential, 1.5 for commercial, and 2.0 for industrial. The Navigant report went on to say that it understood that Union was currently reviewing the appropriateness of those weights. In the undertaking response, Union indicated that it could not find any other 2007 source files related to the weightings. LPMA noted that there was no evidence concerning Union's review anywhere on the record in this proceeding.

LPMA stated that there is no evidence that customer-related costs for commercial customers are 50% higher than they are for residential customers. LPMA noted that customer-related costs include such items as billing and meter-reading costs,

[108] Exhibit H1, Tab 1 at pp. 14-16 (Updated).
[109] Board Staff Submission, August 17, 2012 at pp. 30-34.
[110] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p. 82.
[111] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp.214-217.

depreciation and the return on meters, regulators and service lines. LPMA submitted that Union has provided no evidence to suggest that the commercial customers that would change rate classes under Union's proposal are any different from residential customers when it comes to billing costs or meter reading costs.

LPMA also raised concerns regarding how Union allocated the delivery-related costs for the group of customers that would be changing rate classes under Union's proposal. LPMA noted that these costs include demand-related costs and commodity-related costs. LPMA stated that, in the South, the vast majority of the other delivery-related costs are demand-related costs for both Rates M1 and M2, with a small component of commodity-related costs. In the North, all of the other delivery-related costs are demand-related costs. However, LPMA noted that Union estimated the costs for the customers that are moving rate classes on the basis of commodity volumes. LPMA submitted that a more appropriate methodology would be to use a design-day weighting allocator which is developed based on a full cost allocation study. LPMA noted that Union generally allocates demand-related costs based on peak day demand. However, LPMA noted that Union indicated that based on forecast data it did not have all of the detailed material that is needed to do a detailed cost study.[112]

Parties made differing arguments regarding how to deal with Union's proposal. Many parties argued that Union should be directed to file more comprehensive evidence (including a cost allocation study) supporting its proposal to reduce the volume breakpoint (and specifically supporting the methodology used to allocate costs) in the noted rate classes prior to the Board approving Union's proposal.

Board staff stated that it supports Union's goal to achieve more homogenous general service rate classes and to increase the size of its larger volume general service rate classes. However, Board staff also submitted that Union should file better supporting evidence for the manner in which costs will be allocated between the rate classes that are the subject of Union's proposal.[113]

LPMA and SEC offered other submissions for the Board to consider in adjudicating this issue.

[112] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 85-88.
[113] Board Staff Submission, August 17, 2012, at p. 34.

LPMA submitted that the Board should approve Union's proposal with a modification to the customer weighting, a change to the monthly customer charge, and the direction to file a cost allocation study as soon as possible which confirms that the costs have been allocated appropriately.

LPMA submitted that a more appropriate weighting scheme for the customer-related costs, in the absence of empirical evidence, is to use the same weight for commercial customers as for residential customers. The impact on the customer-related costs that would be moved to Rate M2 is significant. LPMA noted that this change results in a substantial reduction in the costs moved to Rates 10 and M2. The reduction to Rate 10 is $2.4 million and $4.4 million to Rate M2.

With respect to the monthly customer charge for the Rate 10 and M2, LPMA made the following submissions. LPMA noted that Union proposed a $35 monthly customer charge for both rate classes. Union arrived at this monthly charge by taking the midpoint of the monthly customer charges required to recover all customer-related costs for these two rate classes. LPMA stated that this methodology was used to achieve Union’s goal of maintaining the same monthly fixed charge for the noted rate classes. LPMA submitted that Union’s proposal is inappropriate. LPMA noted that there is a clear difference in the monthly customer charge based on the allocated customer charges between Rates 10 and M2. In particular, the cost-based Rate 10 monthly charge would be $41, while the Rate M2 monthly charge would be $30. LPMA stated that Union is effectively under-recovering, based on its proposed $35 monthly charge, from those in Rate 10 and over-recovering from those in Rate M2.

LPMA submitted that the Rate M2 monthly customer charge should be set at $30 and the Rate 10 monthly customer charge should be set at $40. LPMA stated that these recommended monthly charges are cost-based charges.

LPMA submitted that the Board should direct Union to prepare a proper cost allocation study as soon as possible so ratepayers can be satisfied the costs are being allocated appropriately. LPMA stated that the cost allocation study should be filed with the Board and intervenors as soon as possible so the parties have the opportunity to determine if adjustments to rates are required to more properly and equitably recover the properly allocated costs.

LPMA also noted it would be preferable to implement Union's proposal, with its proposed revisions, effective January 1, 2013, rather than waiting until 2014. LPMA noted that Union has indicated that it is not practical to implement the changes by January 1, 2013, as Union requires Board approval in time to update administrative systems and billing systems. LPMA noted that there were no other reasons provided as to why the change could not be implemented on January 1, 2013. LPMA stated that it understands that time may be required to change the blocking structure in Union North to match that of Union South. However, LPMA submitted that there is no reason to delay the change in the break point in Union South. There are no changes proposed in the block structure for Rates M1 and M2. The change in the break point simply requires Union to identify the customers that will move from rate M1 to rate M2, and then move them. As a result, LPMA stated that there is no obstacle to moving a small percentage of the overall customers from Rate M1 to M2 on January 1, 2013. LPMA submitted that the Board should direct Union to implement the remaining change as early as is practical in 2013.[114]

In response to LPMA's argument, Union made the following submissions.

Union noted that the logic of LPMA's position is that there is unlikely to be a significant difference in the customer-related costs to serve residential and commercial customers and as such, these two types of customers should be applied an equal weighting. Union submitted that that logic applies equally to all aspects of the general service, small volume rate class including: residential, commercial and industrial. Therefore, given LPMA's rationale, Union submitted that all residential, commercial and industrial customers should be weighted equally.

With respect to LPMA's argument on the demand-related costs, Union submitted that the methodology used to split the remaining costs is the same as it used to split the costs between the current M1 and M2 rate classes.

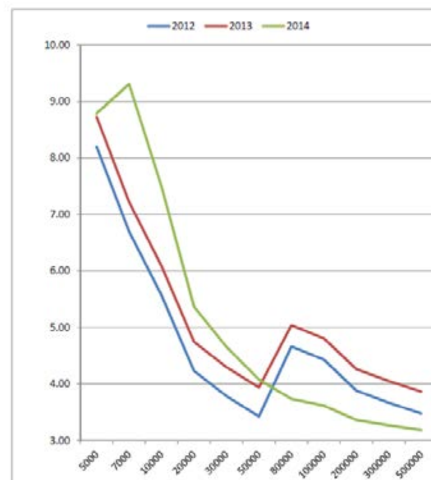
Union submitted that it accepts LPMA's submissions on revising the monthly customer charge to $30 for Rate M2 and $40 for Rate 10.

Union noted that LPMA suggested that the implementation of its proposal occur at the beginning of 2013 for Rates M1 and M2 and that the implementation for Rates 01 and 10 could occur later. Union submitted that this is not possible. Union stated that it needs

[114]Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 85-88 and 90-93.

eight months to change its systems. Therefore, Union stated that it will implement its breakpoint proposal for Rates 01, 10, M1 and M2 in the first QRAM after its systems have been updated to reflect this change.

SEC noted that rate continuity requires that when you go from one rate class to another you would still be recording your economies of scale. SEC noted that in Union North, the rates designed for 2013 and 2014 are relatively continuous and SEC does not have major concerns with rate continuity. However, for Union South, SEC submitted that there are significant discontinuities between rates M1 and M2. SEC provided the following chart which highlights the issues it has raised regarding Union's small volume general service classes.[115]



SEC provided the following analysis of the above chart. SEC noted that the chart reflects the unit costs for customers. SEC noted that when you analyze current 2012 rates and the proposed 2013 rates, at and around the breakpoint there is a large increase in the per unit cost for customers.

SEC noted that there are economies of scale in place as you increase volumes and therefore there should not be any increase at (or around) the breakpoint. SEC stated that the reason for the increased per unit cost around the breakpoint between the M1 and M2 rate classes can only be caused by the fact that there is an over-allocation of costs to the M2 rate class.

[115] SEC Argument Compendium at p. 45.

SEC submitted that the 2014 rate proposal reflects a smoother rate continuum. However, SEC noted that the 2014 proposal still does not address the over-allocation of costs to Rate M2. SEC cited the following table to highlight the over-allocation of costs to Rate M2 and to also comment on its view concerning the over-allocation of costs to Rate 10 in Union North.[116]

	a	b	c	d	e	f	g	h	i	j
	North	*Delivery - related costs*	*Volumes*	*Delivery costs per unit*	*Pre-Move Costs*	*Pre-Move Volumes*	*Pre-Move Unit Costs*	*Post-Move Costs*	*Post-Move Volumes*	*Post-Move Unit Costs*
1	Up to 5,000 (01)	$35,211	609,371,320	$0.057783	$47,065	837,395,959	$0.056204	$35,211	609,371,320	$0.057783
2	5,000 to 50,000 (01-10)	$11,854	228,024,639	$0.051986						
3	Over 50,000 (10)	$15,476	244,955,407	$0.063179	$15,476	244,955,407	$0.063179	$27,330	472,980,046	$0.057783
4	Totals - North	$62,541	1,082,351,366	$0.057783	$62,541	1,082,351,366	$0.057783	$62,541	1,082,351,366	$0.057783
	South	*Delivery - related costs*	*Volumes*	*Delivery costs per unit*	*Pre-Move Costs*	*Pre-Move Volumes*	*Pre-Move Unit Costs*	*Post-Move Costs*	*Post-Move Volumes*	*Post-Move Unit Costs*
5	Up to 5,000 (M1)	$75,911	2,043,883,921	$0.037141	$99,137	2,679,558,627	$0.036998	$75,911	2,043,883,921	$0.037141
6	5,000 to 50,000 (M1-M2)	$23,226	635,674,706	$0.036538						
7	Over 50,000 (M2)	$36,461	971,362,682	$0.037536	$36,461	971,362,682	$0.037536	$59,687	1,607,037,388	$0.037141
8	Totals - South	$135,598	3,650,921,309	$0.037141	$135,598	3,650,921,309	$0.037141	$135,598	3,650,921,309	$0.037141

SEC noted that the above table deals only with delivery costs as the delivery-related costs highlight the issue of the over-allocation of costs to Rates 10 and M2 for 2013.

SEC noted that Line 1 reflects Rate 01, and Line 5 reflects M1. Line 3 and Line 7 reflect Rate 10 and M2 respectively. SEC noted that the delivery costs (on a per unit basis and prior to the implementation of Union's 2014 breakpoint reduction proposal) for a Rate 01 customer are 5.62 cents / m^3 and 6.32 cents / m^3 for a Rate 10 customer. SEC submitted that this cannot be correct.

Similarly, for M1 and M2, SEC noted that the delivery costs (on a per unit basis and prior to the implementation of Union's 2014 breakpoint reduction proposal) for a Rate M1 customer are 3.699 cents / m^3 and 3.753 cents / m^3 for a Rate M2 customer. SEC submitted that this also cannot be correct.

SEC noted that what Union did, in order to adjust for this over-allocation of costs for 2014, is move less costs over for 2014 to achieve a situation where M1 and M2 and 01 and 10, respectively, have the same unit costs for delivery. SEC submitted that this is also likely not correct.

[116] Ibid at p. 61.

SEC stated that because the pre-move costs show higher costs in Rates 10 and M2 that there has been an over-allocation of costs to those rate classes. Therefore, the 2013 costs for the small volume general service classes have been allocated incorrectly. SEC stated that it does not know the quantum of the over-allocation. SEC also noted that the existing over-allocation has only been disclosed because Union has provided evidence regarding the movement of costs in the small volume general service rate classes to give effect to its 2014 breakpoint reduction proposal and it has created some anomalous results.

SEC submitted that considering Union has not done a proper cost allocation study to reflect the new proposed breakpoint, the Board has no way of knowing what the right costs are for 2013. SEC submitted that all that is known, based on Union's evidence, is that the results of Union's allocation are anomalous.

Overall, SEC submitted that the Board does not have the jurisdiction to set new rates for Rates 01, 10, M1 and M2 in 2013, because there is no strong evidence before the Board upon which those rates can be set. SEC submitted that the Board should not change the rates in 2013 for Rates 01, 10, M1 and M2 and should direct Union to file a cost allocation study as soon as possible. SEC stated that the cost allocation study should be filed as part of an application seeking to establish new rates for the above noted rate classes. SEC submitted that any foregone revenues that are caused by not increasing the rates for the above noted rate classes in 2013 should be borne by Union's shareholder as it is Union's responsibility to file sufficient evidence to support changes in rates.[117]

Union argued that there is no legal support for SEC's proposition that the Board has no jurisdiction to approve the rate design changes proposed by Union. Union noted that the Board has the power to set what it determines to be just and reasonable rates.

Union stated that SEC's argument is largely one of rate continuity, which SEC believes to be demonstrative of some inherent problem with Union's allocation of costs.

Union stated that the rate continuity problem raised by SEC has an explanation. Union stated that what has happened during the period of IRM is that the monthly customer charge for rates M1 and 01 were increased from $16 in 2007 to $21 in 2010, and those customer charge increases were offset by reductions in the volumetric rates for these

[117]Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 211-229.

rate classes. Overall, the rate changes were revenue neutral. Union noted that there were no similar increases in monthly charges or corresponding reductions in volumetric rates of the large volume general service classes (Rates 10 and M2). Therefore, Union stated that the rate continuum that existed in 2007 was gradually eroded because of a cross-subsidy that was occurring in the general service rate classes where the larger volume, but still below 50,000 / m^3 customers, receiving the benefit of the reduction in volumetric rates (and not being impacted substantially by the monthly charge increase).

Union submitted that the problem cited by SEC is not a problem with cost allocation. Instead, it shows what can happen with rate design over time and why it is important to monitor these issues. Union submitted that its 2014 breakpoint reduction proposal addresses the concerns raised by SEC regarding rate continuity. Union submitted that SEC's arguments should be rejected and the volumetric breakpoint should be reduced as proposed by Union.[118]

Board Findings

The Board is of the view that Union’s proposal to reduce the volume breakpoint between the Rate 01 / Rate 10 and Rate M1 / M2 classes and harmonize the blocking structure has merit. The Board believes that Union’s proposal does improve the rate class composition of Rate 01 and M1 and achieves more homogeneous rate classes. The Board believes that the proposal will improve the rate class size in Rate 10 and Rate M2, which will ensure viable large volume general service rate classes and improve rate stability.

However, the Board agrees with the submissions of Board staff and Intervenors that the methodology used by Union to allocate costs between the rate classes and give effect to its proposal is flawed. The Board believes that Union’s allocation methodology results in an inequitable allocation of costs as between Rates 01 and 10 and between Rates M1 and M2. As such, the Board will not approve the proposed change in volume breakpoint, effective January 1, 2014.

The Board directs Union to undertake a comprehensive cost allocation study which includes the volume breakpoint reduction proposal. The Board is not satisfied that the allocation has been done correctly at this time and therefore the Board will not accept Union’s proposal. The Board is also not willing to accept LPMA’s proposals to change

[118]Oral Hearing Transcripts, EB-2011-0210, Volume 16 at pp.152-155.

the allocation methodology as there is no evidence on the record that would support a finding that LPMA's allocation methodology is superior to the method put forth by Union.

SEC argued that, if the Board found problems with Union's proposed allocation methodology, it should not change the existing rates at all for 2013. SEC argued that the Board is only empowered to set rates that are just and reasonable, and given that, in SEC's view, Union's allocation of costs as between Rates 01 / 10 and Rates M1 / M2 is flawed for 2013 (even without applying the breakpoint proposal), the Board cannot make any changes to the existing rates (including, a "true-up" to reflect the new Board approved revenue requirement). SEC argued that the onus is on Union to justify any changes to rates, and if its proposals are not adequately supported then the Board should make no changes at all.

The Board does not agree with this position. The Board has an obligation to set rates for Rate 01, Rate 10, Rate M1 and Rate M2 for 2013. Whether the breakpoints remain the same or whether they change, the Board will still set rates for these classes. The Board notes that there was significant criticism of Union's proposed methodology, which may have merit, but the Board will not be changing the breakpoints in this decision. However, this does not lead to a conclusion that the rates in question must be frozen at existing levels. Even if the Board were to keep the rates at existing levels, this would still amount to the setting of rates. To fail to pass along the allocated portion of the revenue deficiency to the 01/10 and M1 / M2 rate classes would result in an unrecovered deficiency for Union. In the Board's view, this outcome would not equate to the Board setting just and reasonable rates.

In setting just and reasonable rates, the Board must make the best determination it can based on the evidence available. Although the Board will not adjust the breakpoints in this proceeding, it will require Union to update the 01/10 and M1 / M2 rates based on the approved revenue deficiency and the other relevant findings in this Decision.

The Board therefore directs Union to file a comprehensive cost allocation study which includes the allocation of costs for its volume breakpoint proposal no later than its 2014 rates filing. The Board directs Union to include in that study analysis of the issue raised by LPMA regarding the allocation of costs for Distribution Maintenance – Meter and Regulator Repairs related to the customers that would be moving rate classes. The Board also directs Union to include an analysis of the Distribution Maintenance – Equipment on Customer Premises cost allocation methodology and an analysis of the

Kirkwall Metering Station cost allocation methodology in this cost allocation study, consistent with the Board's findings elsewhere in this Decision.

Rate M4, Rate M5A and Rate M7 - Eligibility Criteria Proposals for 2014

Union proposed to lower the eligibility criteria for the mid-market bundled contract rate classes (Rate M4 or Rate M5A) and the large market bundled contract rate class (Rate M7) in Union South. Union proposed to implement the bundled contract rate class eligibility changes effective January 1, 2014.

Union noted that it is proposing changes to the mid-market and large market contract rate eligibility for the following reasons:

i. Continuity of service: Lowering the eligibility ensures that existing mid-market contract rate customers will continue to take service in a contract rate class even if they undertake conservation and efficiency initiatives and/or are already at the rate class eligibility threshold.

ii. Sufficient class size: Lowering the eligibility criteria ensures sufficient rate class size for both the mid-market and large market rate classes. Union noted that Rate M7 customers that have already migrated to Rate M4 or Rate M5A as a result of demand reductions will again be eligible for service under Rate M7. The lower eligibility criteria also make a contract rate option available to large non-contract Rate M2 customers.[119]

The proposed eligibility changes for the mid-market and large market bundled contract rate classes are described below.

<u>Rate M4 and Rate M5A – Eligibility Criteria</u>

Union noted that to qualify for service in the current mid-market Rate M4 and Rate M5A rate classes, a customer must have a daily contracted demand between 4,800 m^3 and 140,870 m^3 and a minimum annual volume of 700,000 m^3. In addition, the annual volume commitment for Rate M4 customers must equal 146 days use of firm daily contracted demand (i.e. a 40% load factor).

[119] Exhibit H1, Tab 1 at pp. 28-29 (Updated).

Union proposed to lower the eligibility criteria for Rate M4 and Rate M5A in Union South to a daily contracted demand of 2,400 m^3. The maximum daily contracted demand would be reduced to 60,000 m^3. The minimum annual volume requirement would be reduced to 350,000 m^3. Rate M4 will continue to require 146 days use of firm daily contracted demand.

Union stated that the proposed changes to lower the eligibility criteria for Rate M4 reflect the significant changes in the Union South mid-market. For Rate M4, the number of customers has declined from 194 in the Board-approved 2007 forecast to 121 in Union's 2013 forecast. Union estimated that lowering the Rate M4 eligibility requirements makes a firm contract service potentially available to a further 595 customers with annual volumes exceeding 350,000 m^3 currently taking service under Rate M2.

Union also noted that a large number of customers currently taking service in Rate M4 are at or near the daily contracted demand and annual volume eligibility threshold. Of the 121 Rate M4 customers in the 2013 forecast, there are 31 customers (26%) with daily contracted demand of 4,800 m^3 and 69 customers (57%) whose firm daily contracted demand falls entirely within the first firm demand block of 8,450 m^3 / day.

Union stated that lowering the Rate M4 daily contracted demand threshold to 2,400 m^3 shifts these customers closer to the mid-point of the first demand block, which will allow for more meaningful average pricing and rate stability in this rate class.

Union proposed to lower the Rate M5A eligibility to a daily contracted demand of 2,400 m^3 and a minimum annual volume requirement of 350,000 m^3 to maintain consistent eligibility with Rate M4.[120]

Rate M7 – Eligibility Criteria

Union noted that the current eligibility criteria to qualify for Rate M7 consists of a combined firm, interruptible and seasonal daily contracted demand of 140,870 m^3 and a minimum annual volume of 28,327,840 m^3. Union proposed to lower the Rate M7 eligibility to a daily contracted demand of 60,000 m^3. This minimum daily contracted demand aligns with the maximum daily contracted demand for Rate M4 and Rate M5A.

[120] Ibid. at pp. 29-31

Union proposed to eliminate the minimum annual volume requirement as a condition of qualifying for Rate M7.

Union noted that there are four customers forecast as Rate M7 in 2013. Lowering the Rate M7 eligibility criteria will result in five customers currently forecast in Rate M4 and 17 customers currently forecast in Rate M5A to be eligible for Rate M7. Union stated that at 26 customers, Rate M7 has sufficient rate class size to ensure meaningful average rate class pricing.[121]

LPMA supported Union's M4 / M5A eligibility criteria reduction proposal. LPMA noted that this will offer more M2 customers the option of moving to Rate M4.

However, LPMA noted that it is concerned with the communication that large M2 customers may receive about the movement from Rate M2 to Rate M4.

LPMA noted that the impact on the large M2 customer can be positive or negative, depending on their load factor. Customers with a low load factor could end up paying more under Rate M4 than they did under Rate M2.

Given the uncertainty as to the cost impacts of moving to Rate M4, LPMA submitted that there should be clear and concise communication with customers. LPMA submitted that the Board should direct Union to do a comparison of the annual costs for each of the customers that have the ability to move rate classes, calculating their annual costs based on both Rates M2 and M4. Union should then be required to contact the customer directly and provide them with the information they need to make an informed decision.[122] No other parties commented on this issue.

Union noted that no parties opposed its M4, M5A and M7 eligibility criteria reduction proposal and that it is willing to undertake LPMA's communication proposal. Union stated that it would make sure that the customers know that they will become eligible for contract rate classes at the lower threshold. Union noted that there are about 600 customers that this issue relates to and Union will send a direct mailing to them.[123]

[121] Ibid. at p. 31.
[122] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 93-95.
[123] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at pp. 157-158.

Board Findings

The Board approves Union's proposal to change the eligibility criteria for the mid-market bundled contract rate classes (Rate M4 or Rate M5A) and the large market bundled contract rate class (Rate M7) in Union South. The Board accepts Union's submissions that the proposed changes ensure sufficient class size and the continuity of service in the noted rate classes.

The Board directs Union to communicate these proposals to the relevant customers as agreed to by Union in its reply argument.

Rate T1 Redesign and Rate T3 Customer Charge

Union proposed to split the current Rate T1 into two rate classes with distinct rate structures; a new Rate T1 mid-market service and a new Rate T2 large market service. Union proposed to implement the new rate classes, eligibility changes and rate structures, on a revenue neutral basis, effective January 1, 2013.

Union noted that it made its proposal to split current Rate T1 into two rate classes in order to better align cost incurrence and cost recovery by recognizing the differences in distribution demand and distribution customer-related costs between small Rate T1 and large Rate T1 customers. Union noted that the proposed split also addresses the significant diversity in daily contracted demand and firm annual consumption that exists between small and large customers within the current Rate T1 rate class.[124]

Union also proposed to increase the monthly charge for Rate T3 from $17,657 to approximately $21,661. Kitchener Utilities (the only customer in this rate class) made arguments on this issue, which are discussed below.

Proposed Rate T1 / Rate T2 Eligibility

Union noted that to qualify for the current Rate T1 service, a customer must have combined firm and interruptible annual consumption of 5,000,000 m^3 or more. For the new Rate T1 mid-market service, Union proposed a minimum annual volume of 2,500,000 m^3. Further, Union proposed that the daily firm contracted demand for the new Rate T1 not exceed 140,870 m^3.

[124] Exhibit H1, Tab 1 at pp. 32 and 35 (Updated).

Union noted that the new Rate T2 large market service will be available to customers with a minimum firm daily contracted demand of 140,870 m^3. Union did not propose any minimum annual volume requirement as a condition for qualifying for the new Rate T2.

Union stated that its proposal to split the current Rate T1 into two rate classes will result in improved rate class composition in both Rate T1 and Rate T2. Specifically, both proposed Rate T1 and Rate T2 will be comprised of more homogeneous customers in terms of firm contracted demands and firm annual consumption. The proposed split of current Rate T1 will also recognize cost differences within the current Rate T1 rate class associated with the allocation of distribution demand-related and distribution customer-related costs.[125]

Rate T1 Rate Design and Pricing

Union proposed that the rate structure for the new Rate T1 consist of a monthly customer charge, a two block monthly demand charge and a single block commodity charge. The table below provides a comparison of Rate T1 before rate redesign and proposed new Rate T1 rate structures and proposed rates.

Comparison of 2013 Proposed Rate T1 with no Redesign
and 2013 Proposed Rate T1 with Redesign

	2013 Proposed Rate T1 Firm Transportation Rate with no Redesign		2013 Proposed Rate T1 Firm Transportation Rate With Rate Design Changes	
Monthly Customer Charge	Charge per Re-delivery point	$6,600.83	Charge per Re-delivery point	$2,001.29
Monthly Demand Charge (cents/m^3)	First 140,870 m^3 All Over 140,870 m^3	17.8705 12.2113	First 28,150 m^3 Next 112,720 m^3	31.5395 23.2744
Monthly Commodity Charge (cents/m^3)	First 2,360,653 m^3 All Over 2,360,653 m^3	0.0232 0.0116	All Volumes	0.0715
Fuel Ratio	Transportation	0.237%	Transportation	0.256%

Union noted that the proposed monthly customer charge of $2,001.29 is cost-based and fully recovers all of the customer-related costs applicable to the new Rate T1. The two block demand charge recovers approximately 82% of new Rate T1 demand-related

[125]Ibid at p. 38.

transportation costs. The remainder of new Rate T1 demand-related transportation costs are recovered through the Rate T1 storage related sufficiency. The single commodity charge recovers all the variable transportation costs.

Union noted that the two block demand and single block commodity rate structure for firm service in new Rate T1 is based on the comparable Rate M4 firm service, which also has a daily contracted demand breakpoint of 28,150 m^3. This approach results in consistency between mid-market bundled and mid-market semi-unbundled service offerings.

Union noted that it is not proposing any changes to the storage services currently available under the current Rate T1 rate schedule. However, given that Union is proposing a maximum firm daily contracted demand of 140,870 m^3 in the new Rate T1, the new Rate T1 rate schedule will exclude the storage space, storage injection/withdrawal rights and transportation service provisions that are only applicable to new and existing customers with incremental daily firm demand requirements in excess of 1,200,000 m^3/day.[126]

New Rate T2 Rate Design and Pricing

Union proposed that the rate structure for the new Rate T2 consist of a monthly customer charge, two block monthly demand charge and a single block commodity charge. The table below provides a comparison of Rate T1 before rate redesign and proposed new Rate T2 rate structures and proposed rates.

Comparison of 2013 Proposed Rate T1 with no Redesign
and 2013 Proposed Rate T2 with Redesign

	2013 Proposed Rate T1 Firm Transportation Rate with no Redesign		2013 Proposed Rate T2 Firm Transportation Rate With Rate Design Changes	
Monthly Customer Charge	Charge per Re-delivery point	$6,600.83	Charge per Re-delivery point	$6,000.00
Monthly Demand Charge (cents/m^3)	First 140,870 m^3 All Over 140,870 m^3	17.8705 12.2113	First 140,870 m^3 All Over 140,870 m^3	21.7032 11.3232
Monthly Commodity Charge (cents/m^3)	First 2,360,653 m^3 All Over 2,360,653 m^3	0.0232 0.0116	All Volumes	0.0081
Fuel Ratio	Transportation	0.237%	Transportation	0.234%

[126] Ibid at pp.41-43.

Union noted that the proposed monthly customer charge for the new Rate T2 rate class has been set at $6,000. At this level, the proposed monthly customer charge recovers approximately 50% of the customer-related costs attributable to the new Rate T2. Union proposed to set the monthly customer charge at $6,000 in order to ensure a smooth rate continuum between Rate T1 and Rate T2 at the daily contracted demand breakpoint of 140,870 m^3. Union noted that the balance of the customer-related costs not recovered in the Rate T2 monthly customer charge are recovered in the first block demand charge, which is common to all Rate T2 customers. The revenue-to-cost ratio for new Rate T2 is consistent with the revenue to cost ratio for Rate T1 before rate redesign.

Union noted that the two block demand rate structure for the new Rate T2 is based on a daily contracted demand breakpoint of 140,870 m^3. This is the same daily contracted demand as the current Rate T1 structure. The two block demand charge also recovers all the demand-related transportation costs. The single commodity charge recovers all the variable transportation costs.

Union noted that it is not proposing any changes to the storage services currently available under the current Rate T1 rate schedule. The proposed 2013 Rate T2 rate schedule will include all the current Board approved storage space and storage injection/withdrawal rights per the current approved Rate T1 rate schedule. Union also noted that the transportation service provisions that are applicable to new and existing customers with incremental daily firm demand requirements in excess of 1,200,000 m^3 / day are included in the proposed T2 rate schedule.[127]

APPrO[128] and IGUA[129] supported Union's proposal to split current Rate T1 into two rate classes with distinct rate structures; a new Rate T1 mid-market service and a new Rate T2 large market service.

Kitchener submitted that the proposed monthly charge under Rate T3 is not just and reasonable, relative to the proposed monthly charges for existing Rate T1 (without redesign) and Rates T1 and T2 (with redesign), given the comparability in customer size and load characteristics between large Rate T2 customers and Kitchener.

[127] Ibid at pp. 44-45.
[128] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 142-143.
[129] IGUA Argument, August 22, 2012, at p. 1.

Kitchener submitted that its bears a disproportionate share of customer-related costs under its existing Rate T3 service which are unreasonably (and fully) reflected in the current monthly charge of $17,567 and even more unfairly reflected in the proposed monthly charge of $21,661. Kitchener submitted that these charges are excessive, both in absolute terms and when compared to similarly sized customers in the existing Rate T1 class and proposed new Rate T2 class that, like Kitchener, are directly served from transmission main and do not have multiple redelivery points.

Kitchener noted that while it does not object, in principle, to Union's proposal to split the existing Rate T1 class into a new Rate T1 mid-market service and a new Rate T2 large market service, Kitchener does object to the proposed differential rate treatment for customer-related costs to be recovered under the monthly charge for rates T1, T2 and T3.

Kitchener submitted that the monthly charge under Rate T3 should not exceed the comparable charge for Rate T2 if the Board allows the proposed redesign to proceed. Kitchener submitted that, in the alternative, if the Board does not approve the Rate T1 redesign, then the monthly charge for Rate T3 should not exceed the comparable charge approved by the Board for existing Rate T1.[130]

Union noted that no parties objected to its proposal and therefore it should be accepted. In response to Kitchener's argument regarding the Rate T3 monthly charge, Union submitted that Kitchener had not led any evidence challenging the customer-related costs and the cost allocations in the 2013 cost study, which identified the customer-related costs and those specifically attributable to Kitchener.

Union noted that the proposed T3 rates are increasing by only 2% and the T3 rates have been relatively flat since 2007. Union submitted that this is a reasonable rate increase.

Union stated that Kitchener is requesting that other rate classes pay a portion of Kitchener's customer-related costs. Union noted that it could align the T3 monthly customer charge with either T1 or T2. However, Union would recover the remaining customer-related costs from Kitchener in its demand charge. Union stated that the result

[130] Kitchener Argument, August 17, 2012, at pp. 1-6.

would be that Kitchener's total transportation bill would remain the same. Union submitted that Kitchener's submission should be rejected.[131]

Board Findings

The Board approves Union's proposal to split the current Rate T1 into two rate classes; a new Rate T1 mid-market service and a new Rate T2 large market service effective January 1, 2013. The Board accepts Union's submission that splitting the current Rate T1 into two rate classes better aligns cost incurrence and cost recovery by recognizing the differences in distribution demand and distribution customer-related costs between small Rate T1 and large Rate T1 customers.

The Board finds that the monthly charge proposed by Union for Kitchener, under Rate T3, is appropriate as filed. The Board finds that the proposed monthly customer charge applicable to Kitchener reasonably recovers the customer-related costs incurred to serve Kitchener. In addition, the Board agrees with Union that Kitchener has not challenged the customer-related costs and the cost allocations in the 2013 cost study, which identified the customer-related costs and those specifically attributable to Kitchener. As such, the Board does not have a reasonable basis upon which it could direct Union to revise the T3 customer charge.

Supplemental Service Charge – Group Meters for Commercial / Industrial Customers in Rate M1 and Rate M2

Union proposed to update the additional service charge applicable to "Supplemental Service to Commercial and Industrial Customers under Group Meters" in Rate M1 and Rate M2. Union noted that the supplemental service allows for the combination of readings from several meters, where the meters are located on contiguous pieces of property of the same owner and are not divided by a public right-of-way.

Union proposed to increase the additional service charge on the Rate M1 rate schedule from the current approved $15 per month to $21 per month. On the Rate M2 rate schedule, Union proposed to increase the additional service charge from the current approved $15 per month to $70 per month ($35 per month in 2014 – for consistency with its 2014 M1 / M2 rate design proposal). Union stated that it is proposing to increase the additional service charge to ensure that customers who combine readings from

[131] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at pp. 158-159.

several meters do not receive an unintended benefit in comparison to customers who cannot combine meter readings. This change will result in all Rate M1 and Rate M2 customers paying the same monthly customer charge for all meter readings.[132]

Union noted, in cross-examination, that the benefit received by customers that have the ability to combine meter readings is that those customers have the opportunity to combine volumes. Combining volumes allows customers to have more of their volumes charged at lower rates (in the higher volume blocks of the delivery rates).[133]

VECC supported Union's proposal as filed.[134]Board staff also supported Union's proposal and noted that that the same supplemental charge should be applied in the North. Board staff noted that Union offers an equivalent meter combination service in its Northern service area. However, there is no equivalent supplemental charge.

Board staff submitted that Union's Northern customers that have the ability to combine meters are receiving the same unintended benefit as those Southern customers that have the same ability. Accordingly, a supplemental charge equal to the monthly customer charge should be applied to Union's Northern customers (Rate 01 and Rate 10) that combine meter readings to ensure equitable treatment among the customers in those rate classes.[135]

LPMA submitted that the Board should direct Union to extend its existing policy in the North to the South and eliminate this supplemental service charge.[136]

Union submitted that the longstanding policy in the North of allowing customers to combine meter readings without a supplemental charge should be maintained. However, Union stated that should the Board be inclined to harmonize the supplemental service charge in the North and South, Union supported the introduction of a service charge in the North over the elimination of the South supplemental charge. Union made this argument primarily on the basis that there should not be an unintended benefit for South customers.[137]

[132] Exhibit H1, Tab 1 at p. 56 (Updated).
[133] Oral Hearing Transcripts, EB-2011-0210, Volume 12 at p. 13.
[134] VECC Argument, August 21, 2012, at p. 28.
[135] Board Staff Submission, August 17, 2012 at pp. 29-30.
[136] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at pp. 96-97.
[137] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at pp. 159-160.

Board Findings

The Board finds that the supplemental charge for the combination of meter readings (where the meters are located on contiguous pieces of property of the same owner and are not divided by a public right-of-way) should be harmonized as between North and South. The Board finds that the longstanding policy of allowing customers to combine meter readings without a supplemental service charge should be maintained in the North and should be extended to the South. As such, the Board directs Union to eliminate this supplemental charge in its Southern service area. Accordingly, in the Draft Rate Order process, Union is directed to update its revenue forecast to reflect the above finding.

Rate Mitigation

Union argued that the proposals included in its 2013 rates filing result in total bill impacts of less than 10% and based on the Board's guidelines on electricity, no mitigation is necessary.[138] Union did, however, provide a number of potential rate mitigation measures that could be invoked if the Board deems it necessary. Those rate mitigation measures were provided at Exhibit J11.10.

A number of parties made submissions on the issue ofrate mitigation. Board staff submitted that rate mitigation should only be applied when rate impacts are greater than 10% on the total bill. Board staff noted that 10% rate impacts on the total bill has been used in the past by the Board as a benchmark for what magnitude of rate impacts should trigger rate mitigation for the purpose of setting electricity transmission and distribution rates. Board staff therefore submitted that the same 10% benchmark is appropriate in this case.

If the Board's findings in this proceeding, when taken as a whole, result in rate impacts greater than 10% on the total bill, Board staff submitted that the Board should consider any and all rate mitigation measures it deems appropriate.[139] BOMA supported Board staff's submission on the issue of rate mitigation.[140]

[138] Oral Hearing Transcripts, EB-2011-0210,Volume 13 at p. 81.
[139] Board Staff Submission, August 17, 2012, at p. 34.
[140] BOMA Factum for Argument at p. 54.

Energy Probe submitted that depending on the overall level of rate increases remaining after the Board makes it Decision in this proceeding, rate mitigation measures may or may not be necessary.[141]

LPMA submitted that depending on the Board's findings with respect to Union's M1 / M2 and Rate 01 / Rate 10 volume breakpoint reduction proposal, rate mitigation measures may or may not be necessary. LPMA essentially argued that if the rate impacts for any customer are higher than 10% on the total bill, then rate mitigation should occur.[142]

APPrO submitted that rate mitigation measures should be implemented when the rate impacts are greater than 10% on the delivery portion of the bill, as opposed to total bill impacts.[143] IGUA supported APPrO's position on this issue.[144]

Board Findings

The Board notes that it has made a number of findings in this decision that reduce the revenue requirement and impact the distribution of the approved revenue requirement between customer classes. As a result, it is not clear to the Board at this juncture that rate mitigation will be necessary. The Board will therefore review the rate impacts after the findings set out in this Decision have been implemented in the Draft Rate Order stage of the proceeding. At that time, the Board will determine whether any rate mitigation measures will be required.

Other Rate Design Issues

Board Findings

The Board notes that parties either generally supported Union's evidence or made no comments on the rate design issues listed below.

Issue H2 – Is Union's response to the Board directive to review the M12 and C1 ratemaking methodology appropriate?

[141] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at p. 70.
[142] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p. 98.
[143] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at p. 147.
[144] IGUA Argument, August 22, 2012, at p. 2.

Issue H6 – Is the introduction of M4 interruptible service offering effective January 1, 2014 appropriate?

Issue H9 – Is recovering UFG on transportation activity in the winter months for the Dawn to Dawn-Vector transportation service appropriate?

Issue H11 – Is the proposal to modify the M12, M13, M16 and C1 rate schedules including Schedule A, Schedule A-2013 and Schedule C appropriate?

Issue H12 – Is the proposal to change the Distribution Consolidated Billing fee to $0.57 per month per customer appropriate?

Issue H13 – Are the proposed changes to the Gas Supply Administration Fee appropriate?

Issue H15 – Is the proposal to change the rate design for services originating at Kirkwall to eliminate Kirkwall measuring and regulating costs appropriate?

The Board approves Union's proposals with respect to each of the above-noted rate design issues.

The Board notes that it has included a summary of its findings related to cost allocation and rate design in Appendix "A" of this Decision.

DEFERRAL ACCOUNTS

Average Use Per Customer Deferral Account (Account No. 179-118)

Union noted that the Average Use Account was established in EB-2007-0606 to record the margin variance resulting from the difference between the actual rate of decline in use-per-customer and the forecast rate of decline in use-per-customer included in Union's Board-approved rates.

Union proposed to continue tracking the average use per customer in the existing deferral account. Union also proposed to change the description of Average Use Account in the accounting order to remove the limitation that makes it applicable only to the current incentive regulation plan, 2008 through 2012. Union noted that the proposed

accounting order for the Average Use Account would allow it to be in effect until it is changed or eliminated.[145]

Union initially noted that the Average Use Account will not record differences from forecast for 2013 because 2013 is a cost of service year. The earliest that the Average Use Account would be used is in relation to 2014, assuming that there is an incentive regulation framework in place at that time and that the average use true-up is a feature of that framework.[146]

Energy Probe argued that the average use deferral account should be in operation for 2013 as part of an accommodation for shareholder and ratepayer interests around the 2013 NAC and volume forecasts as discussed in the NAC section of this Decision.[147]

LPMA submitted that it does not accept Union's proposal with respect to the Average Use Account. LPMA noted that this account was established in EB-2007-0606 as part of a true-up mechanism that was utilized under IRM, and the current wording of the account makes it applicable only to the current incentive regulation plan years, 2008 through 2012.

LPMA submitted that this account should not be used for the 2013 test year. LPMA noted that part of the risk for which Union earns its return on equity in a cost-of-service test year is its forecast risk. Use of the Average Use Account would reduce the risk, with no corresponding benefit to customers. LPMA noted that the use of the Average Use Account during the IRM term was to reflect that the average use was expected to decline over the term of the IRM plan, and that both Union and ratepayers would benefit from the implementation of such an account over the IRM, by ensuring that neither party benefited at the expense of the other.

LPMA noted that Union originally indicated that it does not need to keep the account open and that it could be eliminated for 2013 and reintroduced as a part of the next IRM application. In light of the admission, LPMA submitted that there is no reason to keep the account open other than it might be used in 2014. LPMA submitted that the Board should eliminate this account for 2013. LPMA stated that the Board should not approve

[145] Exhibit H1, Tab 4 at p. 3 (Updated).
[146] Exhibit J.DV-4-3-1.
[147] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at p. 51.

the continuation of an account that it knows will not be used for the test year and may or may not be used in the future beyond the test year.[148]

As discussed previously, Union submitted that should the Board have any concerns with respect to the NAC forecast, it could continue to maintain the operation and use of the Average Use Account that was in place during the incentive regulation period. Although Union noted that it does not prefer this approach, it indicated that continuing the Average Use Account would resolve the dispute around the NAC forecast.[149]

Board Findings

As set out earlier in this Decision, the Board accepts Union's NAC forecast as filed, but orders Union to continue the operation and use of the Average Use Account for the 2013 rate year to ensure fairness among Union and ratepayers. The Board therefore directs that the Average Use Account will be open and in operation for the 2013 test year. The Board directs Union to file a Draft Accounting Order for the Average Use Account that reflects the Board's findings in this Decision.

Inventory Revaluation Deferral Account (No. 179-109)

Union proposed to remove the Transmission Line Pack Gas account in the accounting order for the Inventory Revaluation Deferral Account in order to be consistent with accounting changes and for administrative simplicity. Union noted that it has reclassified line pack gas from gas in inventory to property, plant and equipment, and therefore it has proposed that line pack gas should not be revalued quarterly as part of inventory.[150]

LPMA supported Union's proposal and no other parties commented on this issue.[151] Accordingly, Union requested that its proposed change related to the Inventory Revaluation Deferral Account be approved by the Board.

[148] Oral Hearing Transcripts, EB-2011-0210, Volume 15 at pp. 104-106.
[149] Oral Hearing Transcripts, EB-2011-0210,Volume 16 at pp. 25-26.
[150] Exhibit H1, Tab 4, p. 2 (Updated).
[151] Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 104.

Board Findings

The Board accepts Union's proposal to remove the Transmission Line Pack Gas account in the accounting order for the Inventory Revaluation Deferral Account for the reasons cited by Union.

Short-term Storage and Other Balancing Services Deferral Account (No. 179-70)

Union noted that following the NGEIR Decision (EB-2005-0551), Union's practice has been to sell its non-utility storage space on a long-term basis and to sell the excess utility space on a short-term basis (less than 2 years). Union stated that, despite this practice, it is authorized by the Board to sell non-utility storage space under short-term contracts and retain 100% of the revenues.

Union noted that if it sells short-term peak storage services using non-utility storage space, the total margins received from the sale of all peak short-term storage should be allocated to ratepayers and shareholders based on the utility and non-utility share of the total quantity of peak short-term storage sold each calendar year. Union stated that this methodology is transparent to all participants and will yield the same proportionate return on all short-term transactions for the ratepayers and the shareholders.

Union stated that considering the seasonal volatility and variability of market-priced storage, it cannot predict what period of time will yield the highest or lowest prices for short-term peak storage services. Union noted that the use of a proportionate share of calendar year margins ensures that neither party is impacted by the timing of storage sale, or fluctuations to storage values throughout the year.

Union noted that it is able to give effect to its proposal by its ability to track what storage assets are being used for each type of storage transaction.

Union stated that, going forward, it will continue to sell all excess annual utility storage as short-term peak storage and 90% of all margins from C1 Off-Peak Storage, Gas Loans, Enbridge LBA, Supplemental Balancing Services, and C1 Firm Short-Term Deliverability will accrue to ratepayers.[152]

[152] Exhibit C1, Tab 7.

Union noted that it proposed to change the description of the Short-term Storage and Other Balancing Services Deferral Account (the “Short-Term Storage Account”) in the accounting order to update the list of revenues included in the account and the proposed short-term storage margin sharing methodology.[153]

Union proposed the following description for the Short-Term Storage Account:

> To record, as a debit (credit) in Deferral Account No. 179-70 the difference between actual net revenues for Short-term Storage and Other Balancing Services including; Peak Short-Term Storage underpinned by excess utility storage assets, Off-Peak Short-Term Storage, Gas Loans and Supplemental Balancing Services and the net revenue forecast for these services as approved by the Board for ratemaking purposes.[154]

Board staff supported Union’s proposal with a few qualifications. Board staff submitted that Union should sell only short-term storage services using the excess utility space and that the revenues should be allocated between the utility and non-utility storage operations as proposed by Union. With regard to how Union goes about selling short-term services, Board staff submitted that Union should give priority to the sale of short-term storage services that rely on the excess utility storage space. This will help to ensure that ratepayers are not being adversely harmed by Union’s non-utility business selling the same services as its utility business.

In addition, Board staff submitted that the Short-Term Storage Account should capture payments related to storage encroachment. In its January 20, 2012 Decision and Order in EB-2011-0038, the Board stated the following:

> However, the Board does note that, in the past, Union has encroached on its utility space. The Board is of the view that the existence of Union’s utility assets creates a situation where those assets effectively becomean “insurance policy” in relation to Union’s resource optimization activities on the non-utility side of its storage operations. Union’s utility assets can act as a backstop on the rare occasions when Union oversells its non-utility storage space. The evidence suggests that the occurrence of this has been rare and it would be difficult to determine retrospectively to what degree, if any, Union relied on the existence of the utility assets in the conduct of its non-utility storage business to set contract terms and pricing.

[153] Exhibit H1, Tab 4.
[154] Exhibit H1, Tab 4, Appendix C.

> The Board is of the view that there should be an ongoing monitoring of this potential encroachment so as to inform the Board as to the need to revisit this issue at a future date. The Board therefore finds that Union shall be required to monitor for and maintain records of all future encroachments and provide such information in its rebasing application.[155]

It was Board staff's position that the Board, in EB-2011-0038, was concerned about the occurrence of storage encroachment. The Board decided not to address this issue at that time because the occurrence had been rare (only one instance recorded in evidence).

Board staff noted that, in this proceeding, Union provided a schedule highlighting that for a brief period in 2011, Union again encroached on its utility storage position.[156] Board staff noted that this second recorded encroachment requires the Board to address the situation now.

Board staff submitted that Union should be required by the Board to pay fair market value for the use of its utility storage space in the rare situations that Union's non-utility storage operation encroaches on its utility storage space. Board staff noted that in cross-examination Union stated that the cost to rectify its encroachment issue in October 2011 was $1.1 million. This was the cost incurred by Union to move 2 PJs off its system.[157]

Board staff submitted that the 10% incentive payment to Union's shareholder, which applies to the other net revenues in the Short-Term Storage Account, should not apply to storage encroachment payment amounts. Union should not be granted a 10% incentive payment for encroaching on its utility storage space.

Energy Probe supported Board staff's submission and also argued that the account should be broadened to include short-term storage revenues obtained from optimizing utility storage space that is not classified as excess utility storage space.[158]

LPMA noted that there are two issues that need to be addressed related to the Short-Term Storage Account. The first issue is the proposed change in the

[155] Decision and Order, EB-2011-0038, January 20, 2012, at p. 16.
[156] Exhibit C1, Tab 6.
[157] Oral Hearing Transcripts, EB-2011-0210, Volume 7 at p. 173.
[158] Oral Hearing Transcripts, EB-2011-0210, Volume 14 at p. 61.

wording and what is actually to be captured by the account. The second issue is how the amounts that are to be recorded in the account should be calculated.

On the first issue, LPMA submitted that any revenue generated through the use of the regulated utility storage space up to the 100 PJ cap, both planned and the excess over planned, should be recorded in the account for sharing with ratepayers. LPMA stated that to do otherwise would be to deny ratepayers a share of the revenues generated by assets, the costs of which are already built into their rates. The planned use of utility storage assets includes contingency space, some of which is filled on a planned basis and some of which is left empty on a planned basis. The use of the contingency space can be altered during the year depending on the circumstances that exist. Similarly, a colder than expected fall season could result in increased storage capacity being available. LPMA submitted that the wording of the deferral account should reflect the inclusion of all revenues generated from the regulated utility storage assets of 100 PJs.

On the second issue, LPMA submitted that the Board should direct Union to tie all individual transactions to the utility assets first and when all of these assets have been contracted for, only then would any additional transactions be tied to non-utility assets. LPMA noted that Union’s proposal essentially mirrors this, because it is only when the amount of peak short-term storage services contracted for exceeds the excess utility space that the sharing would begin. LPMA noted that the difference between the two proposals is that, under LPMA’s proposal, the prices for the individual transactions would be tied to the utility and non-utility assets, and this methodology should mitigate concerns about Union's potential to capture revenue from utility storage if the value of storage falls during the year.[159]

With respect to Board staff’s argument that the Short-Term Storage Account should capture amounts related to storage encroachment, Union submitted that there is no proper basis for an account to capture amounts related to this issue. Union noted that the last encroachment happened for a very brief period of time and that Union took steps immediately to rectify that situation and incurred a cost of $1.1 million, which was borne in its entirety by Union’s shareholder.[160]

[159]Oral Hearing Transcripts, EB-2011-0210,Volume 15 at p. 109-113.
[160]Oral Hearing Transcripts, EB-2011-0210,Volume 16 at p. 130-131.

Board Findings

The Board believes that there are two issues that need to be addressed with respect to the Short-Term Storage Account. The first issue is the proposed change in the wording in the Accounting Order and what should be captured by the account. The second issue is how the amounts that are to be recorded in the account should be calculated.

First, the Board does not accept Union's proposed wording for the Short-term Storage Account. The Board is in agreement with LPMA that all revenues generated through the use of the regulated utility storage space up to the 100 PJ cap, both planned and the excess over planned, should be recorded in the account for sharing with ratepayers. The Board notes that the revenues that are to be recorded in the Short-Term Storage account relate to the sale of short-term storage, which is defined as all storage transactions that are for a duration of 2 years or less.

The Board also finds that the account should capture storage encroachment and that the 10% incentive payment to Union's shareholder should not apply to storage encroachment payment amounts. The Board believes that there are two issues related to storage encroachment that need to be addressed by the Board in this proceeding.

The first storage encroachment issue relates to the costs arising from actions undertaken to rectify the encroachment, i.e., the cost incurred by Union that is associated with moving gas out of its utility storage space. The Board notes that Union has agreed that its shareholder will pay any costs related to rectifying encroachment situations. The Board believes that this is the appropriate treatment.

The second storage encroachment issue is whether there should be a charge to Union's non-utility storage business to reflect the opportunity cost of the utility storage space that is not available for sale due to encroachment by Union's non-utility storage business. The Board finds that a charge of this nature is appropriate in order to minimize the opportunity for unintended incentives.

The Board notes that pursuant to EB-2011-0038, Union must disclose to the Board when storage encroachment has occurred.[161] That decision, however, only requires Union to file this information in conjunction with its rebasing applications.

The Board therefore directs Union, at the time that the Short-Term Storage Account is to be disposed, to file a report similar to that ordered by the Board in EB-2011-0038. If a storage encroachment has occurred, Union is further directed to file a calculation for the payment by Union's non-utility business to its utility business for storage encroachment. The Board believes that this payment should reflect the market value for the utility space that was subject to the encroachment. The Board notes that this finding only relates to any storage encroachment that occurs after the date of this Decision and will not apply retroactively to previous storage encroachments.

The Board directs Union to revise the wording in the Accounting Order for the Short-Term Storage Account to reflect the above noted findings. The wording in the account must reflect the Board's finding that the account will capture all revenues generated by utility storage assets, i.e., all assets up to 100PJs, and that it will also capture storage encroachment. The Board notes that the Accounting Order shall also be worded broadly enough to ensure that it captures all short-term storage transactions. The Board directs Union to file a revised Accounting Order for the Short-Term Storage Account as part of the Draft Rate Order process.

On the second issue relating to the Short-Term Storage Account, how the amounts that are to be recorded in the account are to be calculated, the Board accepts Union's proposal. The Board believes that Union's proposal to allocate the total margins received from the sale of all peak short-term storage to ratepayers and shareholders based on the utility and non-utility share of the total quantity of peak short-term storage sold each calendar year is appropriate. Given the uncertainty inherent in the pricing of market-based storage, the Board believes that Union's proposal best ensures that ratepayers and shareholders receive the same proportionate return on all short-term transactions.

However, to minimize the opportunity for unintended incentives, the Board directs Union to prioritize the sale of its utility storage capacity ahead of the sale of short-

[161] Decision and Order, EB-2011-0038, January 20, 2012, at p. 16.

term storage services from its non-utility storage operation. The Board finds that whenever utility capacity is available for sale, that capacity is to be used to facilitate short-term storage transactions on a priority basis. Only when utility storage capacity is fully sold can Union sell non-utility storage capacity on a short-term basis.

Finally, the Board directs Union to file sufficient evidence, at the time the balance in the Short-Term Storage Account is to be disposed, to allow the Board to confirm that Union has appropriately prioritized the sale of its utility storage space and calculated the balance in the account in accordance with this Decision.

Gas Supply Optimization Variance Account

Board Findings

In accordance with the Board's findings set out earlier in this Decision, the Board directs Union to establish a symmetrical variance account to capture the variance in the actual net revenues related to gas supply optimization activities and the amount built into rates. As ordered previously, the amount built into rates related to gas supply optimization is 90% of Union's 2013 forecast of base exchanges and 90% of half of Union's FT-RAM 2013 forecast. The balance in the account will be shared 90% to ratepayers and 10% to the shareholder. The Board finds that the balance in this account will be disposed of on an annual basis. The Board also finds that the disposition amounts will be allocated in the same manner as the gas supply optimization related margin amounts will be reflected in rates.

The Board directs Union to file a draft accounting order as part of the Draft Rate Order process which reflects the Board's findings related to the establishment of the Gas Supply Optimization Variance Account.

Gas Supply Plan Review – Consultant Cost Deferral Account

Board Findings

In accordance with the Board's findings set out earlier in this Decision, the Board directs Union to establish a deferral account to capture the costs of hiring a consultant to undertake a review of Union's gas supply plan.

The Board directs Union to file a draft accounting order as part of the Draft Rate Order process which reflects the Board's findings related to the establishment of the Gas Supply Plan Review - Consultant Cost Deferral Account.

Preparation of Audited Financial Statement Deferral Account

Board Findings

In accordance with the Board's findings set out later in this Decision, the Board directs Union to establish a deferral account to capture the costs of preparing audited financial statements.

The Board directs Union to file a draft accounting order as part of the Draft Rate Order process which reflects the Board's findings related to the establishment of the Preparation of Audited Financial Statements Deferral Account.

Elimination of Late Payment Penalty Litigation Deferral Account (Account No. 179-113) and Harmonized Sales Tax Deferral Account (Account No. 179-124)

Late Payment Penalty Litigation (Deferral Account No.179-113)

Union stated that the Late Payment Penalty Litigation deferral account was established in 2004 to record the costs incurred by Union in connection with the late payment penalty litigation. This includes its legal costs, costs of actuarial advice, costs of analyzing historic billing records and the cost of any judgment against Union. Union noted that the litigation in connection to late payment is now complete. Union proposed to close this account effective January 1, 2013.

Harmonized Sales Tax ("HST") (Deferral Account No. 179-124)

Union stated that this account was established to record the amount of Provincial Sales Tax previously paid and collected in approved rates that is now subject to HST tax credits (i.e. the savings to Union). The account was also used to record the amount of HST paid on taxable items for which no tax credits are received (i.e. the additional costs to Union). Union has shared the net impact 50/50 between the ratepayers and its shareholder. Union does not see a need to continue with this deferral account as

Union's budget includes the impact of HST. Upon settlement of the balance in the account, Union proposed to close this account effective January 1, 2013.[162]

No parties raised any concerns arising from the closure of the above noted accounts. Union requested that the accounts be closed.[163]

Board Findings

The Board finds that above noted accounts can be closed as requested by Union. The Board agrees that both of these accounts have served their purpose and are not needed for 2013.

PARKWAY WEST PROJECT

Union's Dawn to Parkway system begins at Union's Dawn Compressor Station and extends 228 km northeast to Parkway, near Oakville, Ontario. The existing Parkway Compressor Station is currently served by a single valve site and header system. The Dawn-Parkway system at this location consists of three parallel pipelines of varying sizes/diameters (26", 34" and 48"). Union connects to the Enbridge system on the suction side of the compressor in the existing Parkway Compression Station. Union owns and operates custody transfer measurement at this interconnection, which is known as Parkway (Consumers).

Union also connects to the TCPL system on the discharge side of the Station in the existing Parkway Compression Station. Union owns and operates check measurement at this interconnection, which is known as Parkway (TCPL). The Lisgar Station is approximately 2 km east of the Parkway Compressor Station. Gas is delivered to Enbridge at the Lisgar Station through 26" and 34" pipelines that extend past the Parkway Compressor Station.

Union has indicated that a significant amount of gas supply intended for delivery into the Greater Toronto Area ("GTA") and other parts of Ontario is either delivered at or passes through Parkway. Based on Enbridge design day system demand of approximately 3.7

[162] Exhibit H1, Tab 4, pp. 4-5 (Updated).
[163] Oral Hearing Transcripts, EB-2011-0210, Volume 16 at p. 131.

PJ/day, Union delivers approximately 57% of that supply to Enbridge at Parkway or through the Parkway compression.

Union has stated that a loss of delivery at Parkway and/or Lisgar would have significant and immediate impact on the Enbridge system. Union indicated that an outage at Parkway (Consumers) would result in a delivery loss of 0.8 to 1.4 PJ/day while an outage at Lisgar would result in a delivery loss of 0.2 to 0.8 PJ/day into the Enbridge system during peak demand. A combined outage of both facilities could result in an immediate delivery loss of 1.6 PJ/day for Enbridge.

Union has indicated that an outage at Parkway (Consumers) and Lisgar during peak demand would impact regional gas flows to points east of Parkway in eastern Ontario, Quebec and the U.S. Northeast as the GTA consumes available supply. In addition, natural gas-fired power generation facilities in the GTA would likely be impacted by low pressure or system outages.

In order to ensure security of supply to its Ontario customers, Union proposes to install a second metering and a header system connected to the Dawn to Parkway system which would allow continued supply to Enbridge in the event of an outage of the existing Dawn to Parkway system interconnection at Parkway.

Union's proposed Parkway West Project is comprised of three components that are to be undertaken over a three year period.

1. Parkway West Land Purchase – 2012: $15.0 million.
2. Parkway West Metering and Headers – 2013: $80.0 million.
3. Parkway West Loss of Critical Unit Protection – 2014: $120.0 million.

The facilities, if ultimately approved, will allow Union to meet export demand on a design day to Parkway (TCPL) and Parkway (Consumers) under an outage of the major components of the existing Parkway compression station.

Union has indicated that the volumes delivered to TCPL through Parkway compression are not fully covered by Loss of Critical Unit ("LCU") protection. According to Union, as volumes grow and throughput through Parkway compression reaches 3.0 PJ/day, there would be no LCU protection. Union has indicated that an outage of one of the Parkway

compressors in the future could significantly impact gas flows during peak demand into Ontario markets, such as the GTA and Northern and Eastern Ontario. Union has stated that failure to deliver during peak day conditions at Parkway could impact the reliability of the Union delivery system and could lead shippers to de-contract on the Dawn-Parkway path. Consequently, Union is of the opinion that LCU protection at Parkway is appropriate and the proposed facilities are the best option.

Union has estimated the cost of the Parkway West Project to be approximately $217 million. Union confirmed at the hearing that none of the facilities would be completed and placed into service during the Test Year. Therefore, the proposed facilities would not impact 2013 rates, and Union stated that it was not seeking any approvals from the Board with respect to the Parkway West Project in the current application.

Board staff submitted that since the project has no impact on 2013 rates, it was not certain what determination the Board could make in relation to this project. Board staff noted that the cost, need, prudence and impact on the environment will all be reviewed in the Leave to Construct application that Union is expected to file before the end of 2012.

Board staff submitted that Union should be directed to file comprehensive information in the Leave to Construct application. This would include detailed information on possible alternatives and the opportunities that the project could provide for the non-utility portion of Union's operations.

Energy Probe submitted that Union had rejected all the alternatives to the project provided by TCPL in its evidence. Energy Probe argued that the Parkway West Project was not just about LCU protection and improving reliability but one of the collateral benefits of this project was that it would increase transactional services at the Dawn Hub. Energy Probe referred to a presentation Union made to Spectra executives that forecasts revenue attributable to the project of $23 million in 2014.

Energy Probe submitted that the Board should conduct a comprehensive review of options for LCU, Parkway extension, Enbridge reinforcements and/or long term transportation arrangements before Union's proposed projects are approved.

BOMA in its submission indicated that apart from the Parkway West Project, Enbridge was planning to construct a 24 km transmission line from the new Albion city gate on its distribution system to Union's proposed Parkway West station. Union and Enbridge initially explored the possibility of joint ownership of the Parkway West to Albion pipeline but Enbridge then decided to construct the pipeline itself.

BOMA submitted that the two distinct projects proposed by Enbridge and Union will likely cost ratepayers more as compared to a joint effort. BOMA was of the opinion that the LCU compression at Parkway was unnecessary at this time and there was no evidence that the new compressor was required to deliver gas to Enbridge or other customers.

BOMA also rejected Union's claim that the LCU compressor was required in the event of a failure of one of the compressors currently in use. BOMA submitted that the likelihood of a serious compression failure was minimal and this was confirmed by Union's evidence on the record.[164]

BOMA noted that Union's evidence of further increases of deliveries through Parkway were not reliable and the market was not ready for such a service at this point in time. BOMA therefore submitted that the Board should forewarn Union about the risk of approval of such expenditures considering that they were not required at this point in time.

BOMA submitted that the Board should examine both the Union and Enbridge expansion plans before it makes a decision to approve either of the projects in and around Parkway. BOMA added that the Board should consider these expansion projects in an Ontario-wide context.

BOMA urged the Board to require TCPL, Union and Enbridge to discuss alternatives and negotiate a solution that minimizes overall capital costs while maintaining reliability and access to markets. BOMA submitted that such discussions should take place prior to Enbridge and Union filing their respective Leave to Construct applications.

[164] Exhibit J.B-1-7-8, Attachment 9, Slide 7.

LPMA in its submission indicated that Union's Leave to Construct application should include a wider perspective: that the needs of Enbridge and the potential options to serve those needs not only by Union, but also by TCPL be considered. LPMA submitted that the Board should consider a proceeding that encompasses Union's Parkway West project, Enbridge's GTA reinforcement project, TCPL options, any Parkway to Maple expansion by any of the companies involved, and any other projects related to this issue. LPMA submitted that the Board's process should include an integrated planning exercise that involves all parties that may be affected, along with all those parties that can provide cost-effective solutions.

APPrO in its submission noted that its members were major shippers on both the TCPL and Union system. APPrO noted that its members were quite sensitive to additional infrastructure considering that TCPL tolls have increased significantly over the last few years.

APPrO maintained that Union should first ensure that there is a genuine problem to resolve and if so, ratepayers deserve the most cost-effective solution and not merely the facility solution that Union has proposed. APPrO submitted that Union should conduct due diligence on potential alternatives to the proposed Parkway West build. This could include not only alternatives proposed by TCPL, but other commercial solutions as well. APPrO recommended that Union conduct broad consultations with all stakeholders including M12 shippers and in-franchise users of the Dawn-Trafalgar system that would be impacted by this major project.

TCPL in its submission maintained that the Parkway West project was at best premature and at worst, a redundant piece of infrastructure that would impose significant costs on Ontario consumers. TCPL submitted that in certain cases, there could be justification for duplicate or redundant infrastructure such as supply diversity and competition. The Board in such cases should weigh the benefits of duplication with the costs that Ontario consumers would bear.

TCPL's opinion was that Union did not require LCU protection at Parkway at this time. TCPL specifically noted that failure of compression at Parkway was an extremely improbable event and that Union's compression has a 99.9% reliability rate. TCPL further noted that two-thirds of the Enbridge GTA peak day load was directly supplied to

Enbridge at Parkway with existing LCU protection and Enbridge was not likely to receive any additional benefit from the proposed LCU.

If Union required LCU protection for TCPL deliveries, TCPL indicated that it could acquire non-facility LCU protection for a fraction of the cost of the $180 million associated with the proposed LCU protection.

TCPL submitted that it had identified at least four alternatives to the proposed LCU which included using existing infrastructure, existing TCPL infrastructure in conjunction with Union infrastructure or adding small and efficient capacity increases on the TCPL system. These alternatives would provide lower ownership and operating costs and would be scalable according to TCPL.

TCPL submitted that Union had not seriously explored all options and had not entered into a dialogue or consultation with TCPL on this matter. TCPL submitted that the project was essentially a way to bypass the TCPL system and had no bearing on providing greater reliability to TCPL or Enbridge at Parkway. TCPL submitted that if the issue is reliability then Union should consult with Enbridge and TCPL to ensure system reliability, both from an operational and economical perspective.

Enbridge in its submission urged the Board to not make any determinations in this proceeding with respect to the Parkway West project including any decisions related to process and timing. Enbridge submitted that any determination would amount to prejudging the Leave to Construct applications that still have to be filed by Union and Enbridge. Union in its reply argument agreed with Enbridge.

Furthermore, Union rejected the alternative proposals put forth by TCPL. Union argued that the alternatives would be more costly if carefully examined and appear largely designed to address competitive concerns that TCPL may have with respect to its own volumes. Union submitted that the proposals put forth by TCPL would either cost more than the Parkway West project or were similar to what Union had proposed. Union submitted that if one of the proposals was simply to install a used compressor, Union could do the same provided TCPL would sell a used compressor to Union. Union noted that in terms of preparedness it was further ahead since it had already entered into an option to purchase the required land in an area where land is difficult to obtain.

Union submitted that Parkway West was essentially a reliability project consisting of two components: LCU protection and a second feed for Enbridge at Parkway (Consumers) and the Lisgar feed backup. Union noted that intervenors were confused about the Parkway West project and were improperly relating it to Enbridge's system reliability project and the expansion of the line from Parkway or Albion to Maple.

Union indicated that TCPL's claim of the Parkway West project being a pre-build for an expansion of Union's transportation corridor was incorrect. Union submitted that the Parkway to Maple congestion was a different issue and Union's position that there is a bottleneck at Maple was well known. Union referred to the presentation that it had given at the stakeholder conference in the Natural Gas Market Review held in October 2010 where it expressed concern about the bottleneck from Parkway to Maple limiting supplies into and from Ontario. In that proceeding, Union had indicated that a Parkway to Maple expansion was a natural project for TCPL to undertake. TCPL in that proceeding disagreed with Union's position and indicated that there was no bottleneck between Parkway and Maple.

Consequently, Union initiated its own open season as a result of which TCPL also held an open season to gauge interest from shippers. In its reply submission, Union confirmed that it bid into TCPL's open season and also indicated that there was insufficient demand for two competing Parkway to Maple projects. Union submitted that there was no evidence that Union was looking to bypass TCPL in this specific corridor.

Union also disagreed with TCPL's claim that it had not consulted with TCPL on the Parkway West project. Union submitted that there was no communication from TCPL and Union learned of TCPL's concern and the different alternatives to the Parkway West project through the evidence filed by TCPL in this proceeding.

Lastly, Union submitted that it is committed to filing complete information in its Leave to Construct application including information about compressors. Union also acknowledged that it assumes the complete risk of expenses incurred on the Parkway West project until it obtains approval for the project from the Board.

Board Findings

In the context of this application, no approvals of the Board are required for the facilities that comprise the Parkway West project. The Board notes that Union plans to file a subsequent Leave to Construct application in the latter part of 2012 for those portions of the Parkway West project that it believes require Leave to Construct approval by the Board. As such, the Board is not making any determination in this Decision relating to the need or any other issue that will be considered in this subsequent proceeding. The Board acknowledges that Union has recognized that any facility expenditures remain the responsibility of Union and its shareholder until, when and if, Board approval is obtained and amounts are closed to rate base.

The record in this proceeding makes it clear to the Board that the relationships between the three large natural gas pipeline companies that serve Ontario customers - Union, Enbridge and TCPL, are complex. The Board notes that not only do these companies compete to construct new facilities and utilize existing facilities; they are also each customers of the other. They are bound, however, by the fact that the operation of each of its respective natural gas system is integrated in the province of Ontario, and that Ontario customers pay a significant portion of, if not all of, the cost of installed natural gas facilities, and that each entity has an incentive to maximize rate base.

The Board is concerned with the apparent lack of cooperation and consultation between Union, Enbridge and TCPL that came to light in this proceeding. The Board is concerned that this may have adverse consequences for Ontario ratepayers – result in higher rates and costs than would otherwise be the case, contribute to the uneconomic bypass of existing natural gas infrastructure, create asset stranding, encourage the proliferation of natural gas infrastructure, and lead to the underutilization of existing natural gas infrastructure.

The Board agrees that the consideration of the Parkway West facilities requires a wider perspective. The Board therefore encourages Union to engage TCPL, Enbridge and shippers in a consultative process, the purpose of which is to jointly consider the need for the Parkway West project, explore reasonable alternatives (including the repurposing of existing facilities) in order to maximize the benefit to Ontario ratepayers. The result of this process would then be filed with Union's Leave to Construct application for the Parkway West facilities.

The Board does not concur with Union's submission that this consultation should occur after it has filed its Leave to Construct application for the Parkway West project. The Board believes that full consideration of alternatives should occur in advance and that to do otherwise would be an inappropriate use of the Board's and other parties' time and resources.

OTHER ISSUES

Financial Statements

Board staff argued that Union should be required to file separate audited financial statements for the rate regulated portion of the company. Currently Union files audited financial statements for the entire company, which includes that portion of its business that is not subject to rate regulation. Board staff submitted that section 2.1.6 of the natural gas Reporting and Record Keeping Requirements ("RRRs") requires Union to file separate financial statements for the rate regulated portion of the utility, and that Ontario Power Generation was required by the Board to file separate audited financial statements for the regulated portion of its business. Board staff further submitted that, irrespective of any requirements in the RRRs, audited financial statements for the rate regulated portion of the business would allow the Board to better assess the revenue requirement and earnings sharing in rate applications.

Board staff's submission was supported by some intervenors. CME noted that separate financial statements for the regulated business would assist parties in determining the proper allocations between the rate regulated and non-rate regulated storagebusinesses.

In reply, Union stated that preparing separate audited financial statements for the regulated side of the business would be an expensive undertaking. It further submitted that no party had identified any particular piece of information that was not disclosed in the proceeding that would have been provided in separate audited financial statements. Union stated that preparing separate audited financial statements would provide little or no value.

Board Findings

The Board directs Union to prepare and file separate audited financial statements for that portion of its business that is subject to rate regulation. For the utility business regulated by the Board, the Board directs Union to provide annually a full set of audited financial statements, with all related notes to these financial statements, prepared under the applicable generally accepted accounting principles used to report to financial regulators in Canada and in the USA. These audited financial statements will be filed with the Board as soon as possible after Union releases its financial results to the public, but no later than June 30theach year. The Board believes that this information will assist in both assessing the revenue requirement in future cost of service proceedings, and in monitoring during the course of the IRM term.

The costs of preparing these financial statements shall be collected in a new deferral account (described in more detail elsewhere in this Decision).The Board will establish a Preparation of Audited Financial Statement Deferral Account, which will be reviewed and disposed of with Union's other deferral and variance accounts.

THE BOARD ORDERS THAT:

1. Union shall file with the Board, and shall also forward to all intervenors a Draft Rate Order attaching a proposed Tariff of Rates and Charges reflecting the Board's findings in this Decision, within 42 days of the date of this Decision. The Draft Rate Order shall also include customer rate impacts and detailed supporting information showing the calculation of the final rates.

2. The Draft Rate Order shall also include draft accounting orders related to the deferral accounts set up or approved by the Board in this Decision.

3. The intervenors shall file any comments on the Draft Rate Order with the Board and forward to Union within 14 days of the filing of the Draft Rate Order.

4. Union shall file with the Board and forward to the intervenors responses to any comments on its Draft Rate Order within 14 days of the receipt of any submissions.

5. The intervenors shall file with the Board and forward to Union, their respective cost claims within 14days from the date of the Final Rate Order.

6. Union shall file with the Board and forward to the intervenors any objections to the claimed costs within 21 days from the date of the Final Rate Order.

7. The intervenors shall file with the Board and forward to Union any responses to any objections for cost claims within 28 days of the date of the Final Rate Order.

8. Union shall pay the Board's costs incidental to this proceeding upon receipt of the Board's invoice.

DATED at Toronto, October 25, 2012
ONTARIO ENERGY BOARD

Original signed by

Kirsten Walli
Board Secretary

Appendix A

EB-2011-0210
Union Gas Limited
Decision and Order

For convenience, the Board's determinations on cost allocation and rate design that have been set out in this Decision and Order are briefly summarized in the table below. However, this summary should not be interpreted as augmenting or superseding any part of this Decision and Order.

Cost Allocation and Rate Design – Summary of Board Findings

Issue	Board Findings
COST ALLOCATION	
General Cost Allocation	Accepted Union's Cost Allocation Study .
System Integrity	Accepted Union's cost allocation proposal.
Tecumseh Metering Assets	Accepted Union's cost allocation proposal.
Oil Springs East Assets	Accepted Union's cost allocation proposal.
New Ex-Franchise Services	Accepted Union's cost allocation proposals related to the Dawn to Dawn-TCPL and Dawn to Dawn-Vector services. Accepted Union's cost allocation proposal for the M12 F24-T service with some required changes.
Union North Distribution Customer Stations Plant	Directed Union to allocate costs related to North Distribution Customer Station Plant on the basis of average number of customers, excluding Rate 01 and the Rate 10 customers that do not meet the hourly consumption threshold of 320 m^3 / hour.
Distribution Maintenance – Meter and Regulator Repairs	Accepted Union's cost allocation proposal.
Distribution Maintenance – Equipment on Customer Premises	Denied Union's cost allocation proposal. Directed Union to file, as part of its 2014 cost allocation study, analysis of this cost allocation issue.
Purchase Production General Plant	Accepted Union's cost allocation proposal.
Parkway Station Costs	Ordered no change to the allocation of Parkway Station costs. Noted that the Board will revisit after Union files the report on the outcome of the Parkway Obligation Working Group.
Kirkwall Station Costs	Directed Union to review its allocation of Kirkwall Station costs as part of its 2014 cost allocation

	study.
Dawn-Trafalgar Easterly Costs	Accepted Union's cost allocation proposal.
Utility / Non-Utility Storage Allocation	Accepted Union's cost allocation methodology. Directed Union to revise allocation for 2012 allocation factor update. Directed Union to file, as part of its 2014 rates filing, continuity schedules related to Union's non-utility storage operation and an update to the Black and Veatch report.
RATE DESIGN	
General Rate Design	Generally accepted Union's rate design considerations and revenue-to-cost ratio guidelines. Ordered Union to not move any in-franchise rate classes' revenue-to-cost ratio further from 1.0 than previously approved. Ordered Union to not have a revenue-to-cost ratio higher than 1.0 for any in-franchise rate class. Ordered Union to file, as part of the Draft Rate Order process, a proposed methodology for allocating optimization related margins to customers that pay the costs of Union's gas supply plan. Ordered Union to file, as part of the Draft Rate Order process, a proposed methodology for allocating S&T related margins which reflects regulatory principles. Ordered Union to update its proposed rates to reflect all of the related findings in the Decision.
Rate 01 / 10 and Rate M1 / M2 – Volume Breakpoint and Rate Block Harmonization Proposal for 2014	Denied Union's rate design proposal at this time. Directed Union to file, as part of its 2014 rates filing, a cost allocation study which includes an analysis of: the allocation of costs for its volume breakpoint proposal, the issue raised by LPMA regarding the allocation of costs for Distribution Maintenance – Meter and Regulator repairs for those customers that move rate classes under Union's volume breakpoint proposal, the allocation of costs for Distribution Maintenance – Equipment on Customers Premises and the allocation of Kirkwall Station costs.

Rate M4, M5A and Rate M7 – Eligibility Criteria Proposals for 2014	Accepted Union's rate design proposals.
Rate T1 Redesign	Accepted Union's rate design proposal.
Supplemental Service Charge – Group Meters for Commercial / Industrial Customers in Rate M1 and Rate M2	Denied Union's proposal. Directed Union to eliminate this supplemental service charge in its Southern Service area.
Rate Mitigation	Noted that it is not clear, at this time, whether rate mitigation will be necessary. Will determine whether rate mitigation measures will be implemented after the Draft Rate Order has been reviewed by the Board.
Response to directive to review M12 and C1 ratemaking methodology	Accepted Union's response.
Rate M4 Interruptible Service Offering for 2014	Accepted Union's rate design proposal.
UFG Recovery on transportation activity, in the winter months, for the Dawn to Dawn-Vector transportation service	Accepted Union's proposal.
Rate M12, M13, M16, and C1 – Rate Schedule Modification	Accepted Union's proposals.
Distribution Consolidated Billing Fee	Accepted Union's proposal.
Gas Supply Administration Fee	Accepted Union's proposal.
Kirkwall to Dawn Transportation Service Rate Design – Kirkwall Metering Costs	Accepted Union's proposal.