DECISION

IN THE MATTER OF an Application by Enbridge Gas New Brunswick Limited Partnership, as represented by its general partner, Enbridge Gas New Brunswick Inc. for approval to change its Small General Service, Mid-General Service, Large General Service, Contract General Service, Industrial Contract General Service and Off-Peak Service distribution rates and for approval of its 2015 Regulatory Financial Statements.

(Matter No. 330)

November 30, 2016

NEW BRUNSWICK ENERGY AND UTILITIES BOARD

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NEW BRUNSWICK ENERGY AND UTILITIES BOARD:

Chairman:	Raymond Gorman, Q.C.
Vice-Chairperson:	François Beaulieu
Members:	Michael Costello
	John Patrick Herron
Counsel:	Ellen Desmond, Q.C.
Chief Clerk:	Kathleen Mitchell

APPLICANT:

Enbridge Gas New Brunswick Limited Partnership:	Len Hoyt, Q.C.

INTERVENERS:

Arauco North America:	Christopher Stewart
Public Intervener:	Heather Black

A. Introduction

[1] Enbridge Gas New Brunswick Limited Partnership, as represented by its general partner, Enbridge Gas New Brunswick Inc. (EGNB or the utility), filed an application with the New Brunswick Energy and Utilities Board (Board) seeking changes to its distribution rates for all classes of customers, except for Off-Peak Service. The classes of customers include Small General Service (SGS), Mid-General Service (MGS), Large General Service (LGS), Contract General Service (CGS), Industrial Contract General Service (ICGS) and Off-Peak Service (OPS). EGNB proposes that changes to distribution rates take effect on January 1, 2017.

[2] EGNB is also seeking approval of its 2015 Regulatory Financial Statements and a ruling on the requirement to continue the retroactive reviews and approval of prior years' regulatory financial statements.

B. Issues

[3] This decision addresses the following issues:

1. The request for the approval of EGNB's 2015 Regulatory Financial Statements;

2. The request for a ruling on the requirement to continue the retroactive reviews and approval of prior years' regulatory financial statements;

3. The request for the approval of EGNB's revenue requirement and proposed changes to distribution rates; and

4. Miscellaneous issues.

C. Analysis

1. Regulatory Financial Statements for 2015

[4] EGNB is currently required to file its annual Regulatory Financial Statements for approval by the Board. The review of the Regulatory Financial Statements for 2015 includes a retrospective assessment of the prudency of spending during that year.

a. Operating and Maintenance Expense Target

[5] In previous decisions, the Board has set an annual Operating and Maintenance (O&M) expense target. In Matter 253, the Board approved a 2015 budget of $11.647 million and a forecasted throughput of 5,846 terajoules. This resulted in an O&M expense target of $1.99 per gigajoule (GJ) for 2015. The actual O&M expense for 2015 was $1.78 per GJ, which is $0.21 per GJ below the Board established target. EGNB has met the O&M expense target for 2015.

b. System Expansion Portfolio Test

[6] Each year, the Board also assesses the prudency of capital expenditures as part of its retrospective review process. This is carried out using a calculation referred to as the system expansion portfolio (SEP) test. In order for capital expenditures to be considered prudent, the SEP test requires that revenues exceed incremental costs by at least 4%.

[7] Mr. Knecht, an expert in the areas of regulatory economics and rate making, filed evidence on behalf of the Public Intervener. As part of his report, he reviewed EGNB's SEP test calculation for 2015. He stated that EGNB's calculations were "conceptually consistent" with established practice for the SEP test. He concluded that the capital expenditures in 2015 passed the SEP test.

[8] In response to an interrogatory, EGNB found inconsistencies in categories of assets between its Excel model and EGNB's accounting system. This resulted in a revised SEP test being filed in this proceeding. The revised SEP test demonstrated that revenues exceeded incremental costs by 48% and, as a result, the Board finds that EGNB passed the SEP test for 2015.

c. Approval of EGNB's 2015 Regulatory Financial Statements

[9] The Board is satisfied that the spending in 2015 was prudent and approves the Regulatory Financial Statements, as filed.

2. Retroactive Reviews of Regulatory Financial Statements

[10] As a result of a Decision dated July 7, 2016, EGNB questioned the necessity of the Board continuing to review prior years' regulatory financial statements. Although this issue was first raised in final argument, no party opposed the request.

[11] The Board finds that parts of the retroactive review, namely the SEP test, are useful on a go-forward basis. There was no opportunity to fully evaluate this issue because it was first raised at the end of the hearing. The Board concludes that further evaluation is warranted and that parties should have a reasonable opportunity to comment.

[12] As a result, the Board will not remove the requirement to continue the retroactive reviews at this time, but will provide direction to the parties at a later date. The parties will be given an opportunity for further input on this issue.

3. Revenue Requirement and Distribution Rates for 2017

[13] The Board is governed by the *Gas Distribution Act, 1999,* S.N.B. 1999, c. G-2.11 (Act) and associated regulations in approving or fixing just and reasonable rates. Pursuant to subsection 4(1) of the *Rates and Tariffs Regulation – Gas Distribution Act, 1999* (Regulation), the Board shall, when approving or fixing just and reasonable rates for each class of customers, adopt the cost of service method, provided that the rates for any class not exceed the rates that would apply to that class of customers if determined through the market-based method.

[14] For the 2016 rate year, the rates for the SGS and MGS classes were approved by the Board using the market-based method. Rates for all other classes were approved using the cost of service method, as their cost of service rates did not exceed market-based rates.

[15] For the purpose of this application, the Board will again review both the cost of service rates and the market-based rates for each class of customers.

a. Cost of Services Rates

[16] The starting point to establish cost of service rates is determining the revenue requirement for the test year. The revenue requirement should provide a reasonable opportunity for EGNB to recover its approved costs, including a reasonable return on prudent investments.

[17] The approved revenue requirement is then allocated among the classes of customers based on a cost allocation study. Once a revenue requirement has been allocated to various classes, rates for each class of customers are established based on forecasts of throughput.

[18] In the following paragraphs, the Board will consider various expenses forming part of the revenue requirement.

i. Corporate Allocations

[19] In a Decision dated July 7, 2016, the Board directed EGNB to establish a filing requirement to review intra-company transactions on a more aggregated basis. EGNB responded to this directive by including a corporate allocations report as part of its evidence in this proceeding.

[20] In response to a question as to whether the review of corporate allocations could be simplified by applying an annual inflationary adjustment, Mr. Lavigne, Senior Manager of Corporate Services for EGNB, testified that this would not allow for any change in the approach to the structure of corporate allocations. He also added that it would not provide the flexibility that the current methodology offers.

[21] Mr. Knecht testified that he was concerned with a percentage adjustment because, over the years, some costs have moved between service level agreements and allocated corporate costs. Mr. Knecht suggested that applying an annual adjustment could inadvertently result in a situation where there might be an incentive to move costs from corporate allocations into service level agreements.

[22] The Board is satisfied that the changes in this application to the evidence relating to intra-company transactions are helpful and approves them, as filed. The Board directs EGNB to continue to file a similar corporate allocations report in future rate applications.

ii. Residential Incentive Program

[23] EGNB has budgeted $100,000 to provide incentives to approximately 50 new customers in the SGS class of customers for 2017. These incentives are applicable to attachments for new home construction, or residential retrofit markets, on or near the current pipeline infrastructure.

[24] A similar program of $100,000 was approved by the Board for 2016. As of October 18, 2016, Mr. Lavigne testified that EGNB spent $33,800 of this amount, covering 18 new residential customers. He testified that the entire approved amount will be spent in 2016. Arauco argued that if the funds are not entirely spent, the balance should be returned to ratepayers in the form of a credit.

[25] Arauco also submitted that the Board should deny the $100,000 sought for this program for 2017, pointing out that the $2,000 incentive only attracted 18 new residential customers with payback periods as long as 38 years. Mr. Stewart, counsel for Arauco, submitted that the system has a problem, that being, the need to control costs. He submitted that giving out incentives to 50 customers is not the answer.

[26] Mr. Knecht noted that given the relatively short time period in which the program had operated, the program should be continued. He recommended that the program be included in the SEP test. Arauco disagreed with this recommendation.

[27] This program was approved last year and there has not been sufficient time to fully evaluate its effect. The Board finds that the program should be continued because it is in the interest of

EGNB and its customers to make prudent investments that expand the system. The Board approves the budgeted amount, as filed, and directs EGNB to include the program in the SEP test.

[28] The Board will continue to monitor and evaluate this program and directs EGNB to present detailed results of this program, as part of its evidence, at the next rate application.

iii. Commercial Customer Retention Program

[29] EGNB is proposing to continue its commercial customer retention program, which began last year. The purpose of the program is to protect the utility's customer base from additional erosion from competitive threats, particularly propane, through the use of incentive payments to at risk customers.

[30] EGNB proposes a budget of $100,000 for 2017. This has been reduced from the $500,000 that was approved in 2016 because the price variance between natural gas and propane is expected to continue to trend favourably.

[31] Mr. Lavigne testified that approximately $196,000 out of the $500,000 has been committed to date, but he expects the entire $500,000 will be spent in 2016.

[32] In Mr. Knecht's view, in light of the short duration of the program and the reduction in the budgeted amount, there is no reason to oppose the continuation of the program.

[33] Arauco argued that the Board should disallow the $100,000 sought by EGNB. Arauco also argued that the approved amount of $500,000 in 2016 was overstated and only $200,000 was necessary. It submitted that any unspent amount in 2016, if any, should be returned to ratepayers in the form of a credit.

[34] EGNB has decreased its budgeted amount from $500,000 to $100,000 for the test year. The Board is satisfied that $100,000 is reasonable for 2017, as competitive threats still exist. Consequently, the $100,000 budgeted for the commercial customer retention program is approved.

[35] The Board will evaluate this program at the next rate application.

iv. Capital Budget

[36] EGNB has budgeted net book value of its capital assets for 2017 at $177,024 million. This is an increase of $3.749 million above its forecast for 2016. Accurately forecasting the amount of

capital additions is important, because it impacts on the estimated interest, return on equity and depreciation expense each year. If the capital additions are overestimated, the revenue requirement may be overstated.

[37] In his evidence, Mr. Knecht concluded that the capital spending is primarily driven by gross new customer forecast additions. He stated that EGNB may be "moderately optimistic" for 2017 about non SGS customers and loads relative to recent historical trends.

[38] At the hearing, EGNB was questioned on the accuracy of the forecasted capital additions for 2017. The utility was asked to explain why the net plant had not grown as expected since 2013 and whether the estimates for 2017 were realistic. On cross-examination, EGNB acknowledged over projections of net plant in 2013 of $93,000; in 2014 of $5.676 million; in 2015 of $4.211 million and in 2016 of $3.304 million for an average of $3.321 million.

[39] In defense of this year's projected capital expenditures, Mr. Lavigne testified that the increase for 2017 includes a couple of specific large projects that are planned in the industrial park in the Hanwell area and an upgrade in the uptown area of Saint John. Dr. Overcast provided evidence on behalf of EGNB as an expert in the area of development of utility cost of service studies and rate design. He testified that urban projects, such as those identified by Mr. Lavigne, are more expensive to develop than suburban projects. He also testified that working in these areas involve multiple utilities on the same street, all of which make it far more expensive for the utility.

[40] The Board finds that EGNB's budgeted capital additions and resulting net plant have been consistently higher than actual since 2013, which has resulted in an average cost of net plant in the revenue requirement being overstated for the past three years. This was confirmed by Ms. Mayo, Manager of Regulatory Finance for EGNB, who testified that the resulting impact on the revenue requirement was, on average, $334,000 for those three years.

[41] As a result of the foregoing, the Board finds, on a balance of probabilities, that EGNB will not achieve the level of capital spending that is forecast for 2017. Notwithstanding that the average impact on the revenue requirement in recent years has been $334,000, the Board is taking into consideration the projects referred to above and finds that it is likely that the utility will underspend its capital budget, although not to the same extent as in recent years. The Board finds that it is reasonable to reduce the revenue requirement by $100,000.

[42] The utility is directed to reduce its 2017 capital budget by an amount that produces a reduction to the revenue requirement of $100,000, taking into consideration the necessary adjustments to return on equity, interest payments, and depreciation.

v. Gas Transportation and Related Activities

[43] The Gas Transportation and Related Activities has been increased by $94,000 in 2017, compared to the 2016 budget.

[44] As part of this expense, EGNB has budgeted, for the test year, an increase in the Maritimes and Northeast Pipeline (M&NP) transportation tolls. These tolls are paid by EGNB for transmission capacity. A 20-year firm service agreement had been entered into with M&NP in 1999.

[45] EGNB was questioned by the Public Intervener on the status of these tolls and whether a firm service agreement had been renegotiated. In response, Mr. Lavigne stated that while no settlement had been reached to date, there had been a number of settlement discussions. He added that EGNB had been provided with potential estimates of the cost of the tolls going forward.

[46] The Public Intervener argued that, since no application by M&NP was before the National Energy Board to increase tolls and the settlement process was not completed, there was no basis to support this addition to the revenue requirement.

[47] The Board finds that Mr. Lavigne's explanation, that EGNB has been in negotiations and has been provided with some potential estimates of the cost of tolls going forward, is reasonable. The estimates provide a reasonable forecast and is the best information available with respect to the gas transportation costs for 2017. Accordingly, the Board approves the amount, as filed.

vi. Cost Cutting Measures

[48] Arauco argued that EGNB needs to continue to be diligent in controlling its costs in order to drive rates down. This is imperative in attracting new customers.

[49] Mr. Lavigne testified that the utility has a cost reduction initiative, including a Lean Six Sigma program, which commenced in 2015. He was unable to report on what savings were achieved in 2016, as the program is in its infancy stage.

[50] The Board agrees with Arauco that it must be satisfied that EGNB is continuing to improve its cost structure to ensure that ratepayers are receiving just and reasonable rates. The Board notes that, in this filing, the overall revenue requirement requested has been reduced from the previous year by $300,000.

[51] The Board concludes that it is necessary for EGNB to continue to demonstrate its commitment to productivity improvement and further reduction of costs. The Board directs EGNB to provide

details of their efforts to reduce costs, including the Lean Six Sigma program, and their results in the next rate application. EGNB should also detail ongoing cost reduction initiatives.

(a) Allocation of Costs

[52] Two issues in relation to cost of service rates were brought forward during the proceeding.

[53] The first issue is whether the technical modifications noted by Mr. Knecht to the cost of service study have merit. The utility indicated that its cost allocation study is consistent with methods used in the past.

[54] Mr. Knecht put forward an alternative cost of service study, which he described to be simpler. He concluded that although “technical internal inconsistencies” existed in the EGNB model, they do not have a material impact in this proceeding.

[55] Dr. Overcast took issue with Mr. Knecht’s proposed model. He stated that Mr. Knecht criticized a model that has been used and accepted in regulatory proceedings for many years. He also took issue with the fact that while simplifying a model may make the process more accessible to those who do not practice cost of service, it also means making assumptions about cost causation that may not be reflective of that fundamental principle.

[56] In final submissions, no party advocated that the Board should make changes to the cost of service model. The Board agrees that no changes are required at this time.

[57] The second issue is whether EGNB’s forecast of test year contract demand for the CGS and ICGS rate classes is consistent with the Board’s Cost of Service Study Decision of December 21, 2010.

[58] EGNB, in forecasting contract demand for the test year, used weather-based design day demands for the CGS and ICGS classes. Arauco argued that this method was contrary to the Board’s Decision of December 2010, which directed EGNB to “use contract demand as the proxy for a class’s contribution where available.” It also argued that the use of contract demand would “materially lower” allocated costs to the CGS and ICGS classes in this proceeding. Arauco requested that the Board direct EGNB to refile its cost of service study, allocating costs in accordance with the Board’s original directive based on contract demand.

[59] In response to Arauco’s arguments, Dr. Overcast testified that using weather-based demand is consistent with the Board ruling of December 2010. He also testified that this is the approach that the utility has used for a number of years since the ruling. As EGNB has been using weather-based contract demand since the ruling, it believes that this is a reasonable approach at

estimating contract demand. He stated that it is the proper representation of what contract demand is in a forecasted test year.

[60] During the proceeding, no questions and undertakings were asked to either expert to recalculate allocated costs to the CGS and ICGS classes using contract demand. No interrogatories were asked on this specific issue. The Board is then left with insufficient evidence to determine a fundamental question in this proceeding, that is, would the use of contract demand "materially lower" allocated costs to the CGS and ICGS classes.

[61] The Board concludes that it should not direct EGNB to refile its cost of service study at this stage of the proceeding, considering that the parties did not fully explore all of the issues relating to contract demand. The Board concludes that the weather-based estimate is an estimate of what the contract demand is during the test year, which is not an unreasonable representation of the contract demand. However, the parties may wish to pursue this issue in a future rate application.

(b) Forecasted Throughput for 2017

[62] Cost of service rates are calculated by dividing the total cost allocated to each class by the forecasted throughput for each class. EGNB filed its forecasted throughput of 5,730 terajoules for 2017.

[63] The Board finds the forecast to be reasonable and approves the 2017 forecasted throughput, as filed.

b. Market-Based Rate Methodology

[64] EGNB is seeking to modify the market-based rate methodology approved by the Board in May 2009. Going forward, the utility proposes to use weather-normalization of annual usage and usage profiles. It argued that weather-normalization is the norm for gas utilities and recognized that these volumes are the best forecast for the test year.

[65] Mr. Knecht agrees with EGNB. He mentioned that since the market-based rates are developed for a future test year that is based on weather normalization, the proposed modification is "sensible."

[66] The Board approves the utility's proposed approach, because weather normalizing the consumption history to determine usage profiles provides more accurate typical customer consumption than using actual loads.

c. Comparison of Cost of Service and Market-Based Methods

[67] In approving or fixing just and reasonable rates, the Board is required to adopt the cost of service method, provided that the rates and tariffs for any class of customers shall not exceed the rates that would apply to that class if determined by the market-based method.

[68] The table below provides the comparison of methods for each class.

Classes of Customers	**Market-Based Rate ($/GJ)**	**Cost of Service Rate ($/GJ)**
Small General Service	12.1121	27.0409
Mid-General Service	12.5639	12.4888
Large General Service	12.2944	4.6229
Contract General Service	8.1141	4.7203
Industrial Contract General Service	8.0098	2.7001
Off-Peak Service	9.4229	2.5766

[69] In proposing rates, EGNB adopted the appropriate methodology for each class of customers as set out in the Regulation. As a result, the Board sets the rates for the SGS by using the market-based method and sets the rates for the other classes by using the cost of service method.

d. Rate Design

[70] In the rate design process, the rates generated by the market-based and the cost of service methods both represent the total costs per GJ to customers. These costs are allocated to customer charges, delivery charges, and demand charges according to the rate design for each class.

i. Proposed Rate Design for 2017

[71] The rate design proposal for 2017 includes the following:

1. Applying a rate increase on the monthly distribution delivery charge for the SGS class;

2. Applying a rate increase on the monthly distribution delivery charge to the MGS class by implementing an increase to the first block, with no increase for the tail block;

3. Applying a rate decrease on the monthly distribution delivery charge to the LGS class by implementing a decrease to the first block, leaving the remaining seasonal tail blocks unchanged;

4. Applying a rate decrease on the monthly distribution delivery charge to the CGS class by implementing a decrease to the winter rate, leaving the summer rate unchanged;

5. Applying a rate decrease on the monthly distribution delivery charge to the ICGS class by implementing a decrease to the winter rate, leaving the summer rate unchanged;

6. Applying a rate increase to the Agent Billing and Collection rates;

7. Making no change to the OPS class; and

8. Retaining the existing fixed monthly customer charges and contract demand charges for all customer classes.

[72] The Board finds that the changes to rate design are just and reasonable and approves them, as filed.

4. Miscellaneous Issues

a. Rate Handbook

[73] The issue of the rate handbook was raised in previous hearings and again in this proceeding. To date, the handbook has not been reviewed for potential improvements and changes.

[74] In this proceeding, EGNB was asked to review its customer service policies and to include any changes in its next rate application. Mr. Lavigne testified that he agreed with this approach.

[75] The Board directs EGNB to review its customer service policies and to make the necessary changes and updates to the rate handbook. These proposed changes and updates are to be filed with the next rate application.

b. Rules of Procedure

[76] In its closing submission, EGNB encouraged the Board to consider reviewing the settlement process currently outlined in the Board's *Rules of Procedure*. All interveners agreed.

[77] The Board agrees that a review of the settlement process may be warranted. The Board will outline a process to undertake this review, and possibly a full review of the *Rules of Procedure* at a future date.

c. Rate Class Review and Assignment

[78] Mr. Knecht examined EGNB's process for its annual rate class customer review. He noted that EGNB uses customers' actual historical loads as the input for the annual review. He raised the question whether EGNB could improve the accuracy and stability of the results by using forecast load or historical weather normalized loads for assigning customers to rate classes. He recommended that EGNB evaluate if budget or weather normalized loads for assigning customers to rate classes would be more accurate and more stable.

[79] In response, EGNB explained that it preferred its approach because it was easier for customers to understand when they asked questions about being shifted to a different class.

[80] The Public Intervener argued that EGNB's response did not answer the question as to whether Mr. Knecht's proposed recommendation might be more accurate.

[81] As EGNB forecasts its load on customer-by-customer basis, the Board finds it may be more proper for the utility to assess its annual rate class customer review based on Mr. Knecht's approach, since it may serve to reduce customer shifting between rate classes and/or provide a more accurate assessment of the classes. The Board directs EGNB to evaluate Mr. Knecht's recommendation and to report on the outcome at the next rate application.

D. Conclusion

[82] The Board finds as follows:

1. EGNB's 2015 Regulatory Financial Statements are approved, as filed.

2. The retroactive reviews and approval of prior years' regulatory financial statements will not be discontinued at this time. Directions allowing parties an opportunity for input concerning this issue will be provided at a later date.

3. The 2017 Revenue Requirement is approved, subject to the $100,000 adjustment pertaining to the capital budget outlined in this decision. EGNB is to refile its cost of service study with this adjustment, proof of revenue and the resulting rates.

4. Once EGNB has filed the necessary additional information, the Board will issue an Order setting out the distribution rates for each customer class. The rates approved in this application will become effective January 1, 2017.

Dated in Saint John, New Brunswick, this 30th day of November, 2016.

Raymond Gorman, Q.C.
Chairman

François Beaulieu
Vice-Chairperson

Michael Costello
Member

John Patrick Herron
Member