DECISION

**IN THE MATTER OF an Application by
Enbridge Gas New Brunswick Inc. for Approval of
its Rates and Tariffs**

June 23, 2000

NEW BRUNSWICK

BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

THE NEW BRUNSWICK

BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

IN THE MATTER OF Section 52 the Gas Distribution Act, 1999, S.N.B. 1999, Ch. G-2.11;

AND IN THE MATTER OF an application by Enbridge Gas New Brunswick Inc. for approval of its rates and tariffs.

Board:	David C. Nicholson - Chairman Léonard Larocque - Commissioner R.J. Lutes - Commissioner Robert Richardson - Commissioner Monika Zauhar - Commissioner
	Lorraine Légère – Secretary M. Douglas Goss – Senior Advisor Carol Nykolyn – Advisor Gary Highfield – Director of Safety John Butler – Consultant James Easson – Consultant William O'Connell - Board Counsel
Enbridge Gas New Brunswick Inc.:	David MacDougall - Solicitor Len Hoyt - Solicitor
Province of New Brunswick:	Ian Blue - Solicitor
Irving Oil Limited:	Christopher Stewart - Solicitor
Sempra Energy Sales Limited:	Peter Zed - Solicitor
Union of New Brunswick Indians:	Juli Abouchar - Solicitor
MariCo Oil and Gas Corporation:	Dennis Holbrook - Solicitor

TABLE OF CONTENTS

PAGE

SUMMARY OF CONCLUSIONS ---------- i

INTRODUCTION ---------- 1

DEVELOPMENT PERIOD ---------- 7

RATES ---------- 10

- TARGET RATES ---------- 10
- RATE RIDERS ---------- 13
- REVENUE-TO-COST RATIOS ---------- 13

CAPITAL STRUCTURE ---------- 15

EXPENSES ---------- 17

- INTRODUCTION ---------- 17
- ADMINISTRATION FEES ---------- 19
- DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT ---------- 20
- AMORTIZATION OF INTANGIBLE ASSETS ---------- 20
- COST OF DEBT ---------- 21
- RETURN ON EQUITY ---------- 25
- INCOME TAXES ---------- 26

DEFERRAL ACCOUNTS ---------- 29

MARITIMES & NORTHEAST PIPELINE ---------- 33

OTHER ISSUES ---------- 40

- AGENT BILLING AND COLLECTION (ABC) SERVICE ---------- 40
- SUPPLIER OF LAST RESORT ---------- 42
- WHOLESALE RATE ---------- 43
- CONTRACT POWER PLANT SERVICE ---------- 45
- UNION OF NEW BRUNSWICK INDIANS ---------- 45
- CUSTOMER INFORMATION ---------- 46
- COMMENTS ON LEGISLATION ---------- 46

INTRODUCTION

The Government of New Brunswick, on December 3, 1998, announced its natural gas distribution policy. The policy provided for three kinds of franchises. A general franchise grants the right to serve the entire province subject to single end use and local gas producer franchises. Single end use franchises would be available for customers who are served directly from the Maritimes and Northeast Pipeline. Local gas producer franchises may be granted to persons who have the right to produce gas in New Brunswick. Any such franchise would be for a specific geographic area.

In December of 1998, the Department of Natural Resources and Energy, , issued a "Request for Proposals to Develop, Design, Construct, Finance, Operate, Manage and Maintain a Privately Owned Natural Gas Distribution Utility" (RFP). Applicants were given until March 31, 1999 to respond to the RFP requesting that they be granted the "General Franchise". Responses to the RFP were to be evaluated by a team of independent experts and senior government officials.

Commercial production of natural gas from the Sable Island field began in 1999. A transmission pipeline was constructed by Maritimes and Northeast Pipeline (M&NP) which extended from Nova Scotia to Massachusetts and commenced operation early in 2000. These two events provided New Brunswick the opportunity to use natural gas as a source of energy.

The Gas Distribution Act, 1999 (the Act) was proclaimed on March 12, 1999. The Act separates the distribution of natural gas from the sale of natural gas. A gas distribution company will construct the pipeline system to transport natural gas to consumers. The natural gas itself is to be sold by gas marketers. The Act requires gas marketers to obtain a certificate from the Board before beginning to sell natural gas in New Brunswick.

The Act provides for the granting of a general franchise to a local distribution company. A general franchise is defined by the Act as follows:

> "'general franchise' means a franchise to distribute gas and provide customer services in the whole of the Province, subject to single end use franchises and local gas producer franchises that have been or may be granted under the former act or this Act. and subject to any order of the Board made under subsection 9(2)"

The Act required that application for a general franchise be made, on or before January 31, 2000, to the Lieutenant-Governor in Council. After that date, any application would be made to the Board.

Two companies submitted responses to the RFP. On August 31, 1999 a General Franchise Agreement (the GFA) was executed granting the "General Franchise" to Enbridge Gas New Brunswick Inc. (EGNB or the Company).

Attached to and forming part of the GFA was Schedule E – Part II Essential Elements. The first paragraph reads as follows:

> “The parties acknowledge that those specific items set out below were relied upon by the gas distributor as being integral to the proposal and constitute fundamental terms of the agreement. The gas distributor and the Province confirm their intention that there should not be any amendment by the Board, in any way, to such items unless the Province and the gas distributor have first agreed to such amendment. These items will apply to and during the Development Period.”

The specific items set out in Schedule E, Part II, effectively described a regulatory environment in which it was proposed that EGNB would operate.

The Board reviewed the "essential elements" and was concerned that their inclusion in the GFA might be interpreted as having fettered the Board's discretion. As a result, the Board wrote to the Minister of Natural Resources and Energy (The Minister) on September 20, 1999. That letter read in part as follows:

> "Although Mr. Barnett's letter, which accompanied the Franchise Agreement, recognizes the Board's jurisdiction and powers, the "essential elements" set out in Schedule E, Part II do not appear to do so. The purpose of writing this letter is to emphasize the Board's opinion that no action of the Executive Branch of Government can override an act of the Legislature. Thus, the discretion delegated by the Legislature to the Board of

Commissioners of Public Utilities can only be altered by the Legislature. The Board must carry out its statutory duties and exercise its discretion in accordance with its constituent statute.

It appears that the government has agreed with the franchisee to the items set forth in Schedule E, Part II. However, these items may or may not be accepted by the Board subsequent to a public hearing at which the Board must decide what is in the Public Interest, after considering all relevant evidence."

The Minister responded on October 4, 1999 and in part stated as follows:

"Please be assured that the Government endorses the autonomy of the Board and recognizes that the discretion delegated to the Board can only be altered by the Legislature. The intent of Schedule E, Part II and the letter from Don Barnett to the Board was to identify the essential elements of the rollout plan submitted by EGNB. Schedule E, Part II underscores the Government's intention to support the fundamental aspects of EGNB's rollout plan and, in doing so, acknowledges the role these elements play in supporting the provincial policy objective to make gas as widely accessible as possible in New Brunswick."

The Board wishes to emphasize that it is fully committed to doing whatever it can to facilitate an orderly, efficient and effective natural gas industry in New Brunswick. The Board has streamlined its regulatory processes where possible and requested parties to provide the necessary information as quickly as possible so that decisions could be made in a timely fashion. It has also established a committee

process to resolve issues outside of the formal regulatory process in an effort to speed up the process and to reduce the cost. The Board remains open to any suggestions that can produce further improvements. In spite of this desire to streamline regulation, the Board has statutory duties pursuant to the Act which it must fulfill.

The Board's task is to balance the interests of the various parties in the natural gas marketplace while carrying out its statutory duties. It must provide an opportunity for the owners of EGNB to earn a fair return on their investment while at the same time ensuring that customers and other parties are protected from any misuse of monopoly power.

The natural gas industry is new to our province. The Board recognizes that the use of traditional regulatory methods may not be appropriate in the early years of developing the industry. For example, full public hearings on all rate changes could add excessively to the costs of regulation. On the other hand, simply allowing EGNB to set rates as it sees fit without some kind of public review would not provide any protection for the other parties.

During the initial years of development, the Board considers that the regulatory framework described in this decision provides the proper balance between minimizing regulatory oversight and protecting the public interest.

EGNB, on December 31, 1999, filed an Application for approval of its rates. On February 7, 2000, EGNB submitted its pre-filed evidence to the Board. A pre-hearing conference was held on February 29, 2000, at which time the procedure leading up to the public hearing was finalized. The public hearing began on April 10, 2000 and was adjourned on April 14, 2000 until April 26, 2000. On April 26, 2000, the parties

presented final argument on the subjects previously addressed. The hearing was then adjourned until May 8 to consider three specific issues, the construction of laterals to connect with M&NP, the assignment of capacity on M&NP and a wholesale rate. Final argument on these issues was presented on May 10, 2000.

The witnesses who testified between April 10-14 were:

Enbridge Gas New Brunswick Inc.

Mr. Arunas Pleckaitas	-	President, EGNB
Mr. Rock Marois	-	Corporate Services Manager, EGNB
Mr. Lino Luison	-	Director, Business & Financial Analysis, Enbridge Inc.
Mr. Allen Maclure	-	Manager, Regulatory Administration, Enbridge Consumers Gas
Mr. Andrew Harrington	-	Manager, Business Development, EGNB
Ms. Pascale Duguay	-	Manager, Rate Research and Rate Design, Enbridge Consumers Gas
Mr. John Thompson	-	Manager, Marketing, EGNB
Ms. Kathleen McShane	-	Consultant

Union of New Brunswick Indians

Mr. Ross Milne	-	Consultant

Irving Oil Limited

Mr. Steve Kirstiuk	-	General Manager Business Development
Mr. Murray Newton	-	Manager, Natural Gas Planning

Board Staff

Mr. Jatinder Kumar	-	Consultant

The following sections provide the Board's decisions on the various issues.

DEVELOPMENT PERIOD

The development period is a term used to describe the amount of time required to move from a "greenfield" situation to a more established natural gas industry.

Currently, there are no customers using natural gas in New Brunswick. For most people it is an entirely new product and they will require time to become aware of its advantages. It is expected that customers will switch from their current energy source to natural gas but the number will initially be small. However, the costs of building the necessary infrastructure will be significant and for several years costs will exceed revenues.

The suppliers of competing energy sources are expected to respond aggressively in an effort to retain their customers. Natural gas is a commodity which trades actively in several "hubs" in North America. There are many sources of and uses for natural gas. The price of natural gas varies in response to market conditions and can rise or fall significantly over a short period of time.

For these reasons, EGNB maintains that it requires the ability to quickly respond to market conditions in order to develop a customer base. Further, it needs assurance that it will have a reasonable opportunity to recover any losses incurred in the first few years of the franchise.

These requirements suggest the use of a non-traditional regulatory framework during the development period. No party to the hearing suggested that this would be inappropriate. The Board considers that a development period, during which a non-traditional regulatory framework would be used, is appropriate.

In its pre-filed evidence, EGNB estimated that the development period would be approximately 8 years, but stated the actual development period would need to be flexible as it is impossible to predict its length accurately at this time. It is clear that the precise length of the development period cannot be established now. The Board believes that it is the appropriate party to make the decision as to when the development period is over. EGNB agrees with this as is shown by the following exchange between Mr. O'Connell and Mr. Marois. (Transcript page 296)

"Q.590 Would you agree with me that the decision-maker as to when the development Period is over is the Board?

A. Definitely."

The Board wishes to minimize the uncertainty associated with the development period so that EGNB can proceed with confidence to develop its distribution system. The Board considers that the development period should last until December 31, 2005. Thereafter, the onus will be on EGNB to annually prove that the development period should be extended for a further year.

There was considerable discussion about the criteria which should be used in determining the cessation of the development period. Customer attachments, rate of return on equity, ability to forecast

accurately, volumes of gas flowing and the economic environment were mentioned as items that should be considered. However, there were no specifics provided that could be used in examining each of these. The following discussion occurred between Mr. O'Connell and Mr. Luison. (Transcript pages 299 – 300)

"Q.595 What about the idea of Enbridge Gas working with Board staff to develop some set of criteria that would give some certainty to the determination of when the development period ends? Is that a reasonable suggestion?

A. I think we have already pointed out that the Board ultimately will decide when the development period is over. We have put in place and put in front of the Board the criteria that we think are relevant for coming to that assessment. We are both starting from scratch with respect to this franchise so, you know, we are clearly open to working with the Board to develop those criteria to the Board's satisfaction so that it can make that decision with whatever information it feels is necessary. So we will, you know, clearly want to work with the Board to come to an agreement on those issues."

The Board considers it appropriate that Board staff, in consultation with EGNB, develop specific criteria that will be used to decide when the development period shall end.

RATES

TARGET RATES

EGNB proposed that a market-based approach be used for setting target rates during the development period. The Company also proposed that rates be on a "postage stamp" basis. This means that the same rate applies to all customers in the same class, no matter where they live in the province. No party objected to either of these concepts.

The market-based approach starts with the premise that the total delivered price of natural gas to the customer must be below the equivalent price for fuel oil. EGNB proposed that its distribution rates be set so that the burner tip cost on an annual basis to the customer would be approximately:

30% below the fuel oil costs in the residential market;

15% below the fuel oil costs in the Light Fuel Oil markets; and

5% below the fuel costs in the Heavy Fuel Oil market.

The starting point, therefore, is to estimate the burner tip prices by rate class for the competing fuel and to apply the appropriate discount. This provides the estimated total delivered price for natural gas to the customer.

The next step is to back out from this total delivered price, by rate class, the forecast costs of the commodity, transportation tolls, load balancing costs and gas marketers' profit margin. The residual amount is the target price, by class, for distribution, that EGNB proposed to charge.

The Board recognizes that there must be an incentive for customers to switch from their existing energy source to natural gas. The Board considers that a market-based approach to establishing the target distribution rates for EGNB is appropriate during the development period. The Board also considers that "postage stamp" rates are appropriate.

EGNB proposed that it would not charge customers any more than the Board approved target rates during a given year. The target rate concept therefore provides a ceiling or cap. EGNB also proposed that it be given the opportunity to adjust the target rates, on an annual basis, to respond to market conditions, if necessary. There were no objections to these proposals. The Board considers that it is appropriate that target rates may be adjusted on an annual basis and that during a given year, target rates will not be increased.

EGNB requested that the target rates filed in its evidence be approved by the Board. EGNB also requested that it be given the flexibility to do a one-time adjustment to the target rates prior to their implementation on October 1, 2000. This exceptional flexibility was requested because market conditions may change considerably by then.

There was considerable discussion, in the cross-examination of EGNB witnesses by Mr. Stewart, counsel for Irving Oil Limited, on the actual values used by EGNB for the various items referred to by the

Company in calculating the target rates. It is clear that, given the time elapsed since EGNB prepared its proposed target rates, the values for certain of the items may have changed significantly. This view is supported by EGNB's desire to be able to change the target rates before October 1, 2000. EGNB stated that the change may decrease or increase the target rates.

The Board considers that the initial target rates should be set on the basis of information that is as accurate and current as possible. It is also important to have rates available as soon as possible so that the marketing of natural gas to customers can begin in a timely fashion.

The expected timing for the release of this decision is such that, if the Board were to approve the target rates as filed, EGNB would need to file any proposed changes to the rates almost immediately after receiving this decision.

The Board does not consider that it would be appropriate to approve rates with the very real possibility that they could be changed in the matter of a few months. It would do little good to the introduction of natural gas in New Brunswick if the rates were to change so quickly, particularly if the change were to result in an increase to the rates that had been previously communicated to customers.

The Board will approve the market based methodology of setting target rates as proposed by the applicant. However, the Board will not approve the target rates as filed. The Board directs EGNB to file proposed target rates that are based on current information together with supporting evidence to show how the value for each item was established. The Board, together with the parties, will establish a time-table for this process. It is the Board's desire to issue its decision on the target rates in time to permit an orderly start to the introduction of natural gas in New Brunswick.

The timing for future reviews of the target rates and the information to be filed by EGNB will be set by the Board after discussions with interested parties. The Board considers that such reviews will be conducted using written questions, answers and comments with an oral hearing only if necessary.

RATE RIDERS

EGNB requested the Board to approve the use of rate riders. A rate rider would be used to reduce the rate for a particular class of customers during a given year. The Company asked that rate reductions be permitted for one or more classes and that more than one reduction be permitted in any given year. The rationale provided was that EGNB needed this pricing flexibility to be able to respond to market conditions. Rate riders would only be used if EGNB believed that the current price was not competitive and further that the price was likely to remain uncompetitive for some time.

The Board considers that the use of rate riders, as proposed by EGNB is appropriate for the development period. The Board will require EGNB to file any proposed rate riders with it and with all marketers at least two weeks before the proposed effective date. The Act requires the Board to approve all rate changes before the new price can be charged. The Board will therefore approve the rate rider as proposed, unless there are exceptional circumstances. The Board will notify EGNB and the marketers of its decision at least one week before the proposed effective date.

REVENUE-TO-COST RATIOS

There was considerable discussion concerning revenue to cost ratios. Mr. Kumar recommended that the revenues and costs associated with each customer class be tracked separately. He also recommended that the revenue to cost ratio for a given class should not exceed 110%.

EGNB's position was that cost of service studies were not appropriate in the early years of a "greenfield" development. Ms. Duguay made the following statement. (Transcript pages 555-556)

> "My opinion about the relevancy of a cost of service study in the initial year of a greenfield project such as the Enbridge Gas New Brunswick project, is that the cost of service study has a very important practical limitation."

The Board agrees that the information that would be provided by cost of service studies in the initial years of a "greenfield" situation would be of limited value. The Board will not require EGNB to file cost of service studies at this time. The Board does consider that the revenues provided by a given customer class should, over time, be reasonably close to the costs incurred to serve that class of customers. This will minimize the amount of cross-subsidy and send the proper economic signals to customers. The Board intends to revisit this issue near the end of the development period.

CAPITAL STRUCTURE

The capital structure of a utility consists of the total of the funds that are contributed by the owners, in the form of equity capital, together with the funds that are obtained by borrowing. The relative proportions of debt and equity in the capital structure are expressed in the form of the “debt to equity ratio”. Where debt and equity are contributed in equal amounts, the ratio is stated as being 50:50.

The “Essential Elements” indicated that the capital structure of EGNB would be on the basis of 50% debt and 50% equity or a 50:50 debt to equity ratio. Mr. Marois stated in evidence as follows:

> “It is important to note that the capital structure we are seeking approval of are not deemed amounts but are based on what is expected to be the actual capital structure…” (Transcript page 71)

Ms. McShane did not give specific support to the 50:50 debt to equity ratio other than to say that it would “…be virtually identical to that maintained by mature…U.S. LDC’s”. (EGNB Evidence, Exhibit C, page 10)

Ms. McShane also provided the capital structure ratios of major Canadian gas and electric utilities. The schedule indicates that the average debt to equity ratio for Canadian gas distributors is approximately 65:35, and that Enbridge Consumers Gas at September 1998 was approximately 71:29.

No objections to the proposed debt to equity ratio were expressed by any intervenors.

Ms. McShane testified that if the Board were to accept a debt to equity ratio including a higher proportion of debt than 50%, the risk for equity holders would be increased and a higher return on equity would be required.

The Board has carefully considered the evidence and finds that the debt to equity ratio during the development period will be based upon the actual ratio of the utility, but that the amount of equity is not to exceed 50 per cent.

EXPENSES

INTRODUCTION

The “greenfield” nature of the natural gas industry in New Brunswick makes it extremely difficult for EGNB to accurately forecast its revenues and costs for the first year of operation.

The prices for the distribution of natural gas are to be market-based and must be responsive to the actions of competitors. EGNB does not control the prices of all the components which make up the total delivered price of gas that customers will pay. EGNB must be able to respond to price changes in the components that it does not control. The target rates may therefore need to be reduced during the year.

The customer attachment rate may be significantly different than that included in EGNB’s proposal to the provincial government. Many people in New Brunswick are unfamiliar with natural gas and their response may be well above or below that anticipated.

The costs to be incurred in the first year depend heavily on the timing for installing the pipe. There is some uncertainty as to exactly when the construction, scheduled for the year 2000, will be completed. In addition, the fiscal year for EGNB may change.

For all these reasons, the specific amounts presented by EGNB as forecasts of revenues, costs and deficiency for the first year of operation may be subject to considerable variation. The Board will use caution in comparing the actual results to these forecasts.

The Board will, as proposed by EGNB, conduct annual reviews of the Company's actual results and forecasts. The first such review will be based on the results up to and including December 31, 2000. The specific information to be provided by EGNB for the review will be determined after discussions between EGNB and Board staff. Interested parties will be given an opportunity to provide written comments on the information which is proposed to be filed. EGNB will be able to respond to any comments received. The Board expects that the list of information required will evolve over time as parties gain experience with the process.

The information filed will be available to the public. The Board will require EGNB to notify its customers annually, by way of a bill stuffer, that they can receive this information from the Company and / or examine it at the Board's offices. Interested parties will be given an opportunity to provide written comments and EGNB will be able to respond to any comments received. The Board will then make a determination as to the amount to be included in the deferral account.

The Board anticipates that the annual review of actual results will be separate from any review of proposed changes to the target rates. The precise timing will be determined by the Board after receiving comments from interested parties.

ADMINISTRATION FEES

The "Essential Elements" indicated that EGNB might be reconstituted as a limited partnership. Mr. Pleckaitis stated that a limited partnership would be established and that a draft Offering Memorandum had been prepared.

The Memorandum indicates that the general partner will be Enbridge Gas New Brunswick Inc. and the partnership will be known as Enbridge Gas New Brunswick Limited Partnership (the Partnership). It also includes details of a Service Agreement between Enbridge Inc. and the Partnership. Under the terms of the agreement, Enbridge will provide the Partnership, directly and through its affiliates, treasury and cash management, administrative, advisory, operating and other services. All such services will be provided at a cost to the Partnership "not to be less favourable…than would be obtainable…in a comparable agreement with a Person that is acting at arms length with the Partnership. In addition,…the Partnership will also pay Enbridge an annual management fee in an amount equal to 1% of the Partnership's expenditures in each fiscal year". (Hearing Exhibit A-16, page 29)

The Board is of the opinion that it is appropriate that Enbridge Inc. and its affiliates be compensated for their efforts by charging market-based rates for all specific services provided. However, the Board orders EGNB to establish the market-based rates on conditions prevailing in the New Brunswick market in all cases where such services could be obtained from local suppliers. Also, the Board orders EGNB to file with it, on an annual basis, details of all services provided by affiliated companies together with the related cost of such services.

Enbridge Inc. and its affiliates will be compensated for all services provided. The Board does not consider it appropriate to require New Brunswick consumers to make any additional payments related to

management of the utility. Accordingly, the Board will not allow the deduction of the 1% management fee for regulatory purposes.

DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

In response to Board Staff Interrogatory #34, EGNB filed details of its classification of property, plant and equipment and its proposed rates of depreciation.

The evidence confirms that the classifications are in accordance with the Gas Distribution Uniform Accounting Regulation. The Board approves of the company using the straight-line method of depreciation and also of the proposed annual rates of depreciation.

AMORTIZATION OF INTANGIBLE ASSETS

Franchise Fee:

In response to Board Staff Interrogatory #21, Enbridge Gas New Brunswick included the franchise fee, stated at an estimated cost of $2,926,065, in rate base. In the forecast years from 2001 onwards, amortization is charged on the basis of a straight-line charge over 20 years, which is the initial term of the General Franchise Agreement.

The Board approves of the amortization of the fee over 20 years.

Franchise Participation Rights Valuation Premium:

The draft Offering Memorandum, at page 43, discloses the payment of amounts by the partnership for all start-up costs incurred by EGNB. The proposed costs include payment of a $4,000,000 “franchise participation rights valuation premium”.

The Board is of the opinion that this payment is strictly an arrangement between EGNB and the limited partnership. It does not accept such payment as a reasonable charge to be recovered from the consumers of New Brunswick. Accordingly, the Board orders EGNB to exclude this cost from rate base for regulatory purposes.

Other Deferred Costs:

The Board recognizes that EGNB has incurred start-up costs that it should be permitted to recover. EGNB has estimated this cost at $4,040,000. The Board will review these costs and permit EGNB to record all reasonable amounts as deferred charges.

The Board will establish the amortization period for these costs at the time of the first review of EGNB's results.

COST OF DEBT

The cost of debt of a utility is the rate of interest charged by debt-holders on the funds borrowed by the utility. The total cost of debt may also include other contributing factors such as costs incurred in the issuing of the debt and foreign exchange variations.

The “Essential Elements” indicated that the return on, or cost of, debt for EGNB will be the 10 year Government of Canada bond rate at the time the debt is incurred, plus 2.5%.

In her evidence, when addressing the issue of cost of debt, Ms. McShane stated as follows:

> “The debt will be loaned to Enbridge Gas New Brunswick via intercompany loans on terms and conditions that Enbridge Gas New Brunswick would incur if it were to raise the debt on its own behalf in the public markets”. (EGNB Evidence, Exhibit C, page 10)

During the hearing, witnesses on behalf of the applicant consistently maintained that EGNB should be regulated as a “stand-alone” entity without regard to the existence of its parent and affiliated companies.

Ms. McShane stated as follows:

> “The imputation of the stand-alone cost of debt to Enbridge Gas New Brunswick’s operations based on Enbridge Gas New Brunswick’s risk ensures there is no cross-subsidization between Enbridge Gas New Brunswick and its parent, i.e., that Enbridge Gas New Brunswick is not being subsidized by the customers of any of the parent’s other operations, regulated or unregulated”. (EGNB Evidence, Exhibit C, page 11)

The evidence established that there is a very close relationship between EGNB and its parent and affiliated companies. Mr. Pleckaitis stated:

> “It means that in the starting up of a corporation, one of the things that we benefit from is being able to draw people, experienced people from elsewhere in the corporation to help them with certain aspects of starting up our company. These are people that already have existing skills in operating a regulated utility”. (page 245 of the transcript)

Mr. Luison testified:

“And if I can just add to that, the reason we do that is because there are certain skill sets and activities that have to be performed front end…we just staff up as is required at the front end”. (Transcript page 246)

"Q.467 And Enbridge Gas New Brunswick has the benefit of being a wholly-owned subsidiary of Enbridge Consumers Energy Inc. with all the expertise and talent that goes with that?" (Transcript page 246)

"A. Right. And presumably that was one of the reasons that I guess we won the bidding process, was because we were able to establish to the government’s satisfaction that we did have the know-how and the experience to carry on with this…sort of a greenfield project." (Transcript pages 246-247)

"Q.469 You convinced the Province of New Brunswick that they weren’t dealing with just Enbridge Gas New Brunswick but with the Enbridge group…with all the resources and talent and expertise that comes from a hundred years…in this industry, correct?" (Transcript page 247)

"A. Yes. That’s correct." (Transcript page 247)

Ms. McShane testified:

"Q.223 Do you know if the execution of the general franchise agreement by the Province of New Brunswick and Enbridge Gas New Brunswick had any impact on the bond rating of Enbridge Consumers Gas or Enbridge Inc.?

A. I doubt it. It's not big enough." (Transcript page 670)

Based upon the evidence, the Board is unable to accept the argument that EGNB should be considered as a "stand-alone" entity for purposes of establishing its cost of debt.

In establishing a fair cost of debt for the inter-company loans to EGNB by its parent, Enbridge Inc., the Board has considered the following evidence. Enbridge Inc. will be borrowing funds on the market at the rate of interest consistent with its bond rating.

In response to Province of New Brunswick interrogatory #35, Ms. McShane indicated that the then current yield on 10-year Government of Canada bonds was 6.2%, and that Enbridge Inc. had raised debt in early March 2000 at 6.815%. She further indicated that this cost of debt represented a 67 basis point spread over the 10-year Canada benchmark.

Advancing funds to EGNB at 10-year Canada rates plus 2.5% results in a spread of approximately 1.8% over the cost to Enbridge Inc. The Board is of the opinion that this would provide a benefit to Enbridge Inc., which is excessive in the circumstances.

The Board understands that EGNB is entering a greenfield situation which inherently carries a risk that the market will not develop satisfactorily. Therefore, there must be a premium to compensate Enbridge

Inc. for this risk. Accordingly, the Board orders that the cost of debt of EGNB be limited to the actual borrowing rate of the parent company plus 1%. This rate is to apply to both long-term and short-term borrowing. In addition, the Board orders EGNB to record all the information necessary regarding the borrowing cost of its parent company in support of its interest charges to EGNB.

RETURN ON EQUITY

The return on equity of a utility is the rate of return allowed to be earned on the capital invested by shareholders in the enterprise, expressed as a percentage of such capital. The percentage is normally calculated by reference to the cost of "risk free" capital in the money markets, to which a premium is added, based upon the perceived risks of the particular enterprise. The latter component is known as the "risk premium".

The "Essential Elements" stated that the return on equity will be 13% during the development period. Ms. McShane expressed her opinion that the rate of return of 13% was reasonable and supported her opinion with an analysis of the forecast of long Canada yields and the required risk premium for Enbridge Gas New Brunswick.

Mr. Kumar gave no opinion on the appropriate return on equity. No intervenors objected to the rate of 13% established in the company's application and no proposed alternative rate was developed.

The Board finds that the rate of 13% is to be the return on equity allowed during the development period. However, the Board orders EGNB, in the event of actual earnings exceeding 13% during the development period, to apply all such excess as a lump sum payment in the reduction of the deferral account.

INCOME TAXES

The "Essential Elements" indicate that "In the event that EGNB is reconstituted as a legal partnership, applicable taxes will be deemed to be all those taxes which would have been payable by a corporation".

It is the Board's understanding that this section of the application means that when calculating the revenue requirement for a test year, the return on equity of 13% is to be calculated after a notional charge for corporate income taxes.

In response to Board Staff Interrogatory 10, Mr. Luison confirmed that the taxes to be included in the cost of service are the taxes which would have been paid by a corporation.

The impact of income taxes is discussed in the Offering Memorandum (Exhibit A-16) on pages 35 and 36 as follows:

> "The return on equity of the Partnership increases steadily from an initial annualized rate of 7.4% in 2000, to 24.5% in 2007. This reflects the gradual shift in the equity deployment of the Partnership from investments earning 6.3% to utility equity providing the pre-tax equivalent of 13% after tax. However, because of the tax deductions generated during the start-up of the Gas Distribution Utility, the cost-of-service regulatory regime does not recognize the payment of any deemed taxes by the Partnership, or their recovery as a cost-of-service, until 2005 and increasingly thereafter."

Ms. McShane had no comments in her evidence with reference to the proposed inclusion of deemed income taxes in cost of service.

Mr. Kumar in his evidence commented as follows:

> "However, the partners would be investing the money in the partnership in expectation of their profits net of income taxes. Thus the cost of capital to EGNB would reflect this expectation. To collect taxes on a hypothetical basis would be a windfall to EGNB and its partners". (Kumar Evidence, page 59).

Later, he indicated that:

> "In all probability, EGNB will have tax losses for many years, whether it incorporates or operates as a limited partnership. Therefore, for the years of tax losses, no income tax allowance should be included in the rates". (Kumar Evidence, page 59).

The Board has carefully considered this evidence and notes that the general partner considers that it is unlikely that EGNB will be in a position where, as a deemed corporation, it will have taxable income before 2005.

The Board notes that if EGNB were to remain as a corporation it would obviously be required to pay income taxes. Therefore, the customers of EGNB will be no worse off with EGNB operating as a partnership and having income taxes deemed as if EGNB were a corporation.

Although customers will be no worse off, the partnership arrangement will permit New Brunswick citizens to invest in EGNB. This will provide the benefit of a certain amount of local control and involvement.

Therefore, during the development period, the Board approves of the inclusion of deemed payable income taxes in the cost of service, on the basis that would have prevailed, in any year, as if the partnership had been a corporation.

DEFFERAL ACCOUNTS

EGNB proposed that it be allowed to establish two deferral accounts, a Pricing Deferral Account (PDA) and a Forecast Discrepancies Deferral Account (FDDA). It also requested that these accounts be amortized over a 40-year period and that the balance in the accounts would earn the weighted average cost of capital allowed for EGNB.

EGNB indicated that the PDA would consist of two components;

1. the deficiency caused by the Target Rates being established at a level that did not recover the full cost of service, and
2. the deficiency resulting from the Actual Rates being lower than the Target Rates after Rate Riders had been used during the year.

The FDDA would be used to accrue the differences between "…actual and forecast revenues and cost of service (not taking into account any rate reduction that EGNB had to make to the Target Rates during the year which will be captured in the Pricing Deferral Account)…" (EGNB Evidence, Exhibit A, page 14)

EGNB summarized its position as follows:

1. these accounts can conceptually be viewed as one account,

2. revenue from any source will essentially go to reducing the deferral accounts,
3. a return equal to EGNB's weighted cost of capital would be paid to the customers on any positive balance, and
4. a positive balance in one account will be netted out against any negative balance in the other account.

Irving Oil Limited (Irving) accepted the need for deferral accounts, but suggested that the Board should not allow these accounts to be accepted without question. EGNB should be required to defend all expenditures as used and useful and to justify all amounts accrued in these accounts. "The Board should establish a procedure through which the levels of the deferred account balances, and the reasons and prudence of those levels that have been achieved, can be examined by the Board and other stakeholders." (Exhibit C-23, page 11)

Irving considers deferral accounts to be deferred income. It accepted that carrying costs should be allowed on the balances in these accounts, but suggested that EGNB should not be allowed to use them as profit centers. Irving recommended that the Board ensure that EGNB has an incentive to keep the balances as low as possible. There should be no incentive to make them higher than necessary. To accomplish this, Irving proposed that the carrying costs allowed on the balances in these accounts should be at the Board approved cost of debt only.

Irving also expressed concern with the term over which these accounts will be amortized, suggesting that this will have an impact on rates for the indefinite future.

The revenues from the gas distribution system in New Brunswick will be insufficient in the early years to cover the investment by EGNB. Therefore, the Board accepts that EGNB should be allowed to defer costs incurred during the early years for recovery over a future period.

The Board has concerns with the use of multiple deferral accounts. A review of the purpose of these accounts reveals that in total they will accrue the difference between the actual revenue received and the calculated revenue requirement for a full cost of service. EGNB's proposal can be viewed as merely dividing this total amount among the different accounts.

In most jurisdictions, the regulatory agency approves the use of deferral accounts when changes occur that are outside the control of the utility. The balances in the accounts can generally be traced to specific events or the actions of specific customers and/or customer classes. The balances are ultimately either collected from, or returned to the specific customers or customer classes based on cost causality. In this case, although the deferral accounts proposed by EGNB are to accommodate circumstances beyond its control, neither account can be identified with the occurrence of specific events or the actions of specific customers or customer classes.

Both EGNB witnesses and its counsel stated that, conceptually, these accounts could be viewed as one. The Board can find no justification for separating these accounts, particularly for regulatory purposes. EGNB is directed to establish one deferral account in which it will record the difference between the actual revenue received and the revenue requirement approved by the Board.

EGNB requested that the amount deferred should be amortized over forty years so as to minimize the impact on rates. The Board is concerned that such a long period of amortization will not necessarily be

in the best interests of the customers. The Board therefore requires that EGNB establish an amortization schedule, at the end of the development period, that will clear the balance in the deferral account over the remaining term of the initial General Franchise Agreement.

The Board accepts that to allow only the approved cost of debt on the balance in the deferral account would result in a reduction in the allowed rate of return on EGNB's investment. EGNB will be allowed to accrue a return on the average balance for each fiscal year equal to the overall rate of return as approved by the Board.

MARITIME AND NORTHEAST PIPELINE (M&NP)

The Enbridge Gas New Brunswick (EGNB) distribution system must be connected to the M&NP interprovincial pipeline in order for customers in New Brunswick to receive natural gas. This connection requires an interconnecting pipeline referred to as a lateral together with custody transfer stations.

EGNB's distribution network required to serve Moncton/Riverview/Dieppe (Moncton), Fredericton/Oromocto (Fredericton) and St. George require a lateral at each location. A custody transfer station is required for each of these three laterals and four stations are required off the M&NP lateral to serve Saint John, for a total of 7 stations.

It is the policy of M&NP that it must build the custody transfer stations. EGNB has reluctantly accepted this policy in order to permit the timely development of the natural gas industry in New Brunswick. It is noted that this policy has not been formally adopted by the National Energy Board (NEB) which is the federal agency with regulatory oversight of M&NP. It was also clear on the record of this proceeding that the costs of the seven stations to be built by M&NP significantly exceed the cost estimated by EGNB to build the stations itself. No party in this proceeding objected to M&NP building these particular facilities. The Board therefore considers that it is appropriate for M&NP to build the seven custody transfer stations. The Board strongly encourages EGNB to pursue, before the NEB, the possibility of it being permitted to

build any future custody transfer stations itself. The Board also encourages the NEB to closely scrutinize the costs of M&NP in the construction of both the custody transfer stations and the laterals in light of EGNB's cost figures presented to this Board.

EGNB stated that its overriding objective was to reduce capital expenditures and expenses associated with the construction of the laterals and thereby reduce the size of the deferral account balances. However, with respect to the Fredericton lateral, EGNB also considered the effect on its ability to serve customers. After weighing these two objectives, EGNB decided it was preferable to build this facility itself. No party objected to this approach. The Board will accept EGNB's proposal to construct the Fredericton lateral.

EGNB's position was that it is preferable for M&NP to build the Moncton and Saint George laterals. Again, no party objected to this approach. The Board considers that it is appropriate for M&NP to construct the Moncton and St. George laterals. The cost of the seven custody transfer stations will be included with the cost of the laterals. EGNB presented two options with respect to paying for the combined cost of the two laterals and the seven stations.

One choice was a contribution in aid-to-construct. This would require an upfront payment of $12.2 million. This approach would not provide EGNB with any transportation capacity on the M&NP system.

The second choice was to enter into a firm service agreement (FSA) with M&NP. This would require annual payments of approximately $3 million for twenty years and provide transportation capacity on the M&NP system of 11,785 gigajoules (GJ) per day for the 20 year period of the FSA. EGNB is not permitted to sell gas except as a supplier of last resort. In the FSA option, EGNB would market its capacity

rights on the M&NP system to gas marketers, single end use franchisees and other shippers on M&NP located in New Brunswick as well as other jurisdictions. Any revenues from the sale of this capacity would be used to reduce the costs to the ratepayers of EGNB.

The contribution in aid-to-construct approach would require that the ratepayers of EGNB make payments sufficient to amortize the $12.2 million. They would also be required through rates to pay the interest, income taxes and return on equity associated with the unamortized amount of the $12.2 million payment. There was discussion at the hearing of the possibility of EGNB being responsible for property tax payments associated with the facilities in question. However, EGNB stated that the facilities would be owned by M&NP and that EGNB had not gone to the Province for a ruling on this issue. Mr. Marois stated that the net present value to EGNB of the contribution in aid-to-construct was $19 million. Although no detailed study was presented in evidence by EGNB, it is clear that this amount includes annual payments for property tax. The Board doubts that this should have been included in the calculation as real property taxes are normally assessed against the owner of the property.

The FSA approach would require ratepayers to pay approximately $3 million per year for 20 years. This amount of $3 million would be reduced each year by the amount of revenues received from the sale of the capacity that EGNB owned on the M&NP system. Mr. Marois provided an estimate of $26 million as the net present value for the annual payments associated with the FSA. This amount did not include any allowance for staff costs required to monitor market conditions and to negotiate sales.

The precise cost to ratepayers for the contribution in aid-to-construct approach is not clear from the record. However, it is clear that it is less than the cost of the annual payments under the FSA method. However, the FSA does provide an opportunity to reduce the cost through the sale of capacity. EGNB

stated in its pre-filed evidence that it is reasonable to assume that over time 60-75% of the capacity costs could be recovered. Mr. Marois, under cross-examination, stated that EGNB believes it can beat the target of 50% recovery of capacity. In summation, the Province of New Brunswick maintained that the uncontested evidence is that EGNB expects to sell 65-70% of the FSA capacity. At these levels of cost recovery, it is clear that ratepayers would be better off with the FSA approach than the contribution in aid-to-construct approach.

It is also clear on the record that there is considerable risk associated with the sale of capacity by EGNB. The market for natural gas is new to New Brunswick and will evolve over time. In response to Board staff interrogatories, EGNB stated that it did not have a forecast of revenues from the sale of capacity and that the price and length of contract for capacity would be best set by the marketplace. The Board considers that the sale of capacity will occur in a market where numerous buyers and sellers are trading. It is therefore extremely difficult to predict the actual amount of revenue that will be provided by the sale of capacity over the 20 year period of the FSA.

The marketing or sale of capacity by EGNB and the terms and conditions under which such sales should occur was a topic of considerable discussion at the hearing. EGNB's strong preference was to have considerable, if not complete flexibility with respect to the sale of capacity. EGNB, in response to Irving interrogatory number 5, stated "that it is essential that it is able to keep all options open for the release of its capacity in order to maximize cost recovery."

In summation, Counsel for Irving suggested the following ground rules relating to the sale of capacity:

1. The process must be open, public and transparent

2. No prearranged deals unless the full toll is recovered
3. Notice of sale of capacity must be given, and
4. Sales of capacity should be limited to a two year term.

EGNB stated that it would provide information to the Board annually with respect to the sale of capacity during the previous year. However, EGNB did not consider it appropriate to report, in advance, to the Board at the time of each sales transaction. If required to do so, it maintained that this would seriously limit its flexibility and impact negatively on its ability to maximize sales revenues and thereby reduce the overall cost.

The Board has carefully considered all evidence presented concerning the sale of capacity by EGNB. The Board believes that such sales will occur in a competitive market. Such a market requires EGNB to be able to respond quickly in order for it to be as effective as possible. It is not reasonable to require each potential deal to be submitted to the Board for review and approval. Any such review would require information on the currently available options and an informed assessment of the options that might reasonably arise in the future. The Board does not consider that it would be appropriate for it to conduct such reviews. For the same reasons, it considers any review of the sale of capacity by EGNB to be of little value. It encourages EGNB to conduct its sale of capacity in a manner that is as open and transparent as possible, including the possible use of an electronic bulletin board. The Board believes that Section 69 of the Act provides a basis for parties to file complaints if they consider that any sales of capacity by EGNB have occurred in an inappropriate manner. It believes that the interests of ratepayers will be best served by allowing EGNB to market its capacity rights on the M&NP system without any specific constraints imposed by the Board.

EGNB requested that the Board approve the inclusion of the financial commitments of the FSA in its cost of service for the life of the contract. The Board has carefully considered this request in light of the risk associated with the sale of capacity. The comments provided suggest that it would not be unreasonable to expect that 50% or more of the costs will be recovered. However, there is obviously no guarantee that this will occur. This uncertainty is highlighted by the following:

Mr. Marois, under cross-examination by Mr. O'Connell, stated that EGNB would not be prepared to arrange for capacity on the M&NP system if this were to be treated as an unregulated part of the business. The Chairman asked "if the Board were to…allow 35 percent of the cost to flow into your rate base, would you then be prepared to have it an unregulated service for that 65 percent?" (Transcript page 1356) Mr. Maclure responded: "I think that we would want to do a fair bit of thinking about the extent to which we would want to enter into that agreement." (Transcript page 1356)

The Board believes that it is appropriate to establish a mechanism, which will provide a balance between the interests of EGNB's ratepayers and shareholders with respect to the risk associated with the sale of capacity. The Board will therefore allow EGNB to include in its cost of service each year 50% of the annual payment to M&NP. This amount will be adjusted each year by one-half of the amount by which the revenue from the sale of capacity differs from $1.5 million.

For example, if revenue equals $1.5 million there would be no adjustment. The ratepayers would pay $1.5 million. This together with the sales revenue of $1.5 million would provide for the $3 million payment to M&NP.

If revenue were only $1 million the ratepayers would pay an additional $0.25 million ($1 million less $1.5 million equals $0.5 million which divided by two equals $0.25 million) for a total charge of $1.75 million. This, together with sales revenue of $1 million, provides $2.75 million. The remaining $0.25 million necessary for the $3 million payment to M&NP would be provided by the shareholders of EGNB.

If revenue were $2 million, the ratepayers would benefit by $0.25 million ($2 million less $1.5 million equals $0.5 million which divided by two equals $0.25 million). Their total charge would therefore be reduced to $1.25 million. This amount together with the $2 million of sales revenue would provide a total of $3.25 million. After the payment of $3 million to M&NP this would leave $0.25 million for the shareholders. This $0.25 million of profit would be over and above the allowed return on equity.

OTHER ISSUES

AGENT BILLING AND COLLECTION (ABC) SERVICE

EGNB is offering the ABC Service as an option to all gas marketers. Under this service, EGNB will bill customers for gas supply charges on behalf of the marketer and it will also be responsible for collection from the customer. Since EGNB will be billing customers for distribution services, this service will result in the customers receiving only one bill.

EGNB is planning on outsourcing part of this service to its parent company Enbridge Consumers Gas (ECG) in Toronto. The rates it will offer marketers in New Brunswick are the same as ECG offers in Ontario. The proposed charges for this service are as follows:

Small General Service (SGS)	$1.05/bill
General Service (GS)	$2.00/bill
Contract General Service (CGS)	$5.00/bill

EGNB will pay ECG for the Agent Billing component of the service at $0.85/bill for SGS customers, $1.63/bill for GS customers and $4.06/bill for CGS customers. The additional amounts of $0.20/bill for SGS customers, $0.37/bill for GS customers, and $0.94/bill for CGS customers is based on the Ontario experience and it will be collected by EGNB to cover the cost of bad debt.

EGNB witnesses stated that the marketer would always be paid in accordance with its agreement with its customers. In some cases the marketer could be paid for gas supply before EGNB has billed the customer for that gas. EGNB stated that it will bear the full collection risk from customers for all marketers who elect to take this service.

Although EGNB is requesting Board approval of the above rates for its ABC Service, it also indicated that it "…will need the flexibility to adjust these charges in the future as costs and market conditions dictate." (EGNB Evidence, Exhibit A, page 16)

Irving notes that this is an optional service, but suggests that since the objective should be to encourage marketers to come into this area, this rate should be as low as possible. It also recommends that the rates for this service should be a straight pass through from ECG to the marketers, without any mark up by EGNB.

Irving pointed out that these charges require Board approval. It suggested that if EGNB proposed to increase these charges in the future that marketers must be given notice, with the right to object. If the rates generate too much revenue, possibly as a result of bad debts being lower than forecast, then EGNB should be required to lower the rates as an encouragement to marketers. Irving argued that EGNB should not be allowed to make a profit from the provision of this service.

No intervenor objected to either the provision of the service or the rates that are proposed by EGNB. The Board approves both the service and the rates as proposed, but will require that EGNB annually file information related to this service. EGNB will file sufficient information each year on the

revenues and costs resulting from this service to justify both the continuation of the service and the level of the rates. EGNB must file an application for any changes to the rates for ABC service.

The Board is concerned that the ABC service is only offered as a bundled service with one charge for all three components. It suggests that EGNB consider changing this rate so that marketers have the option to be responsible for the collection of bad debts. This would allow those marketers who wish to provide their own bad debt coverage to do so, thus avoiding EGNB's charge for that service.

SUPPLIER OF LAST RESORT

The Act only permits EGNB to sell natural gas in the event that a gas marketer fails to supply gas to a customer on a timely basis and no other gas marketer is able or willing to do so. In this instance, EGNB acts as or arranges for a supplier of last resort service.

At Exhibit B of this application, EGNB proposed a Last Resort Supply Service rate which was calculated to be 110% of the full replacement costs of the gas delivered at city gate. In a response to an interrogatory, EGNB elaborated on the rate components. It explained that the full replacement cost of the gas would include the cost of the commodity, fuel and transportation. In addition, other activities such as making contractual arrangements with third parties to acquire the gas, monitoring and billing would need to be performed. The 110% was set arbitrarily by EGNB to compensate for the activities directly related to the provision of the Last Resort Supply Service that are in addition to the full replacement costs.

No party opposed EGNB's Last Resort Supply Service rate or offered an alternate rate design.

The Board has reviewed EGNB's proposal and accepts that the Last Resort Supply Service will only be provided by EGNB on an emergency basis. Basing the rate on 110% of the full replacement costs is reasonable for this service. The Board will approve EGNB's proposed rate for the Last Resort Supply Service.

WHOLESALE RATE

In its proposal to the Province, EGNB provided illustrative rate schedules and a rate handbook which included a wholesale rate. However, its rate application to the Board did not include a wholesale rate.

EGNB provided the following reasons to justify its dropping of the wholesale rate. The contractual relationship with the end use customer would be different under a wholesale rate. The marketer, contracting as principal with EGNB, would eliminate EGNB's direct relationship with the end user. EGNB raised the issue of safety and stated that it would have a reduced ability to communicate directly with the end use customer when it only knows the location of the initial service connection as opposed to the identity of the end use customer. Wholesale service would remove the distributor from being the initiator of disconnection procedures and would mean that the marketer would bill end use customers for EGNB's distribution charges. The marketer is not regulated and therefore, the Board would not have the authority to regulate the distribution rates charged by the marketer.

Irving argued that a wholesale service would permit marketers to offer a one stop shopping option to customers giving them the simplicity of having all natural gas services dealt with by the marketer. This would encourage more customer conversion to natural gas, which would be beneficial to the customer, the marketer, and EGNB. If the Board were concerned that it would no longer have the authority to regulate

the contents of the bill for distribution rates, Irving stated that the Board could control the contents of a marketer's bill through its marketer's certification process. Irving also stated that it would bill each customer the same distribution rate that the customer would be charged if it were billed directly by EGNB. This would ensure that distribution rates continued to be on a postage stamp basis. The same rate would apply to all customers in the same rate class no matter where they lived in the province and whether they were billed by Irving or EGNB.

EGNB argued that Irving's proposal was not a wholesale service but rather a billing scheme. The Company believed that this was an issue which had been dealt with at the Marketers' Hearing. EGNB stated that Irving had challenged EGNB's proposed sole right to bill end use customers for distribution service at the Marketers' Hearing and failed. EGNB maintained that Irving's wholesale service proposal in this proceeding was simply a repackaging of their approach to billing.

EGNB's argument was supported by the Province of New Brunswick and Energy Source Canada. No other intervenor commented on this issue.

The Board considers Irving's wholesale service concept to be a marketing strategy that simply provides a single bill option for the customer enabling a marketer to bill for EGNB's distribution services and its own services. The provision of billing services and the question of who should provide billing services was determined by the Board after the Marketers' Hearing. Therefore, the Board will not require EGNB to offer a wholesale service at this time.

CONTRACT POWER PLANT SERVICE

EGNB has requested Board approval of a customer class identified as Contract Power Plant Service. The application states "The Rate for service shall be determined for each Applicant based upon the costs imposed upon the Company to provide the requested service." The Board will approve this class of customer but EGNB must file an application with the Board requesting approval each time EGNB plans to offer this service to a customer. The application must provide all relevant information on the costs and revenues that would be associated with the particular customer.

UNION OF NEW BRUNSWICK INDIANS (UNBI)

The UNBI advised the Board in its summation that negotiations had been initiated between EGNB and the UNBI with respect to concessions to be made to the aboriginal people, including training, job opportunities, and the protection of medicinal plants and sacred sites. Its purpose in intervening in this hearing was to ask the Board to approve the inclusion in EGNB's cost of service of all costs associated with the negotiation of an agreement and all costs to EGNB resulting from any agreement.

The UNBI claimed it had researched regulatory practice in the US and Canada and had found no instances of regulators refusing to include such costs in the cost of service for a utility. However, no examples were provided of Canadian regulatory tribunals who had specifically approved the inclusion of such costs in the cost of service for any utility. Examples were provided from the United States and Columbia, showing that regulators had included specific provisions for first nations in those countries.

The Board will not approve, in advance, EGNB including an unknown amount of expenditure for an, as yet, unspecified purpose in its cost of service. The onus is on EGNB to prove to this Board that any

costs it wishes to include for regulatory purposes are reasonable, that they have been prudently incurred, and that they are necessary for the operation of the gas utility.

CUSTOMER INFORMATION

EGNB's market-based approach for setting target rates during the development period allows EGNB the opportunity to adjust the target rates on an annual basis. This approach also provides a ceiling or cap as EGNB may only reduce its rates below the target rates during the year.

The Board is concerned that new gas consumers might think their distribution rates are regulated in the traditional manner. To avoid this, customers must be given clear notice, prior to receiving service from EGNB, that their rates are market-based rates, and are subject to change after a specified notice period. This message must be repeated annually with the notice of any target price changes to ensure that customers remain aware of this term of service. The Board directs EGNB to work with Board staff in preparing these notices to customers.

COMMENTS ON LEGISLATION

This is the first time that the Board has had an appropriate opportunity to comment on the Act since its passing in March, 1999. In the Board's opinion, the Act is a progressive regulatory tool. However, there are a few sections that the Board believes must be amended in order for the natural gas market to develop in an orderly fashion in the Province.

It is obvious to the Board that the Legislature wished to have the monopoly local distribution company (EGNB) regulated by the Board. The Board is free to use whatever form of regulation it deems appropriate. It is further evident that the Legislature wished to have the sale of the commodity occur in an

open competitive market place. It is also plain that the sale of customer services, as defined in legislation, should occur in that same open competitive market place.

The Board's regulatory responsibilities concerning the marketers of gas and of customer services were restricted to reviewing an application for a certificate based upon the criteria set forth in Section 62. This section only requires that the applicant be financially responsible and show past conduct which does not indicate undesirable business practices. Once these criteria are met, the Board must issue a certificate. It is in the light of this understanding of the scheme of the Legislation that the Board wishes to comment on three specific problems.

1. **<u>The Definition of Gas Marketer</u>**

Section 58 requires the Board to issue a certificate to every Gas Marketer. The definition of Gas Marketer includes a person who "(a) sells or offers to sell gas or a customer service to a customer". The definition of customer service is "a service that is not a natural monopoly and includes appliance service, yardline or houseline maintenance, meter reading, billing, collections, call center, load balancing, peaking service, supplier of last resort service, storage and arranging for pipeline capacity on a transmission line or a pipeline regulated by the United States Federal Energy Regulatory Commission"

This Board questions why persons selling the following customer services should have to be granted a certificate by the Board to compete in an competitive market place: appliance service, meter reading, billing, collections, call center, load balancing, peaking service, storage and arranging for pipeline capacity.

It is this Board's opinion that by the inclusion of these services in the definition of customer service and thereby requiring a Board certificate, the Act is imposing an unwarranted degree of regulation on the delivery of customer services in the natural gas industry. In addition to increasing regulatory impediments to entry in the market place, the process of issuing certificates will increase the administrative costs of the Board which will have to be borne by natural gas customers.

2. **Assessment Provisions**

Section 87(4) of the Act reads as follows:

"The Board shall assess each gas distributor and gas marketer;

(a) its direct expenses, and

(b) its share of the common expenses, which shall be determined according to the proportion the gross earnings of that gas distributor or gas marketer bears to the aggregate of the gross earnings of all gas distributors or gas marketers to which this Act applies".

The Board does not criticize the framers of the Legislation. However, in modeling this section after the assessment provisions of the Public Utilities Act, we believe the provisions of this section to be simply unworkable in the natural gas industry for the following reasons:

1. Unless the definition of "gas marketer" is amended, the Board must ascertain the gross earnings of every person that, not only sells gas, but offers a "customer service". This would be a monumental task and add further regulation and barriers to market entry to an industry where open competition is intended to exist.

2. Even if the Act were amended to remove providers of customer services from the definition of gas marketers, the Board is of the opinion that those who sell gas would still find the assessment provisions to be inequitable. The gross revenues of a gas seller will include the price of the commodity and the cost of transport on the transmission line. Thus, it appears likely, in aggregate, that the sellers of gas will have greater gross revenues than will the local distribution company. The gas sellers will therefore pay a greater proportion of the Board's annual assessment than will the regulated local distribution company. It is the opinion of the Board that the sellers of gas in an open competitive market place should not pay the lion's share of the regulator's cost.

The Board believes that the possibility of gas marketers (gas sellers) having to pay the lion's share of the Board's cost is mitigating heavily against gas marketers entering the New Brunswick market place. Experience elsewhere indicates that gas marketers operate on a very thin margin. The additional unknown cost of assessment by the Board could well result in a prospective gas marketer not entering the New Brunswick market place. This may lead to a lack of competition in the New Brunswick natural gas market.

The Board recommends that the assessment section be amended. The first preference is to amend it so that the local distribution company (LDC) would pay all of the Board's assessment each year. The customers will pay for this through the LDC's rates. If this is not acceptable to the Legislature, then the second preference is an amendment that gas sellers not pay any portion of the Board's assessment until such time as the market matures. This could be at the end of the development period. Until the development period ends, the gas distributor would pay all of the Board's costs.

If neither of the two preceding options are acceptable to the Legislature, the Board suggests that the amendment give it discretion to decide what portion of its common expenses will be recovered from gas distributors and what portion from gas marketers. The distributor's portion would then be assessed against each distributor based on the proportion its gross earnings bears to the total gross earnings for the group. The marketer's portion would be assessed against each marketer based on the proportion its sales, in cubic meters, bears to the total sales in cubic meters.

Finally in reference to assessment, the Board notes the Select Committee of the Legislature recommended that the annual “single end-use franchise fee” be used to reduce the cost of regulation. The Board supports this recommendation and notes that receipt by the Board of the annual $250,000 would cover over two thirds of the Board’s estimated cost of providing safety inspection services for local gas distribution in this province.

3. **Definition of “Pipeline”**

In the Act “pipeline” is defined as “any pipe, system or arrangement of pipes wholly within the Province for distributing gas and all property and works of any kind used in connection therewith but does not include a pipeline for which a permit has been issued under the Pipe Line Act or a transmission line”. Subsection 25(1) states “A gas distributor shall not operate a pipeline unless it holds either a licence or a provisional licence granted by the Board under subsection (2)”. Subsection 25 (2) states “After a pipeline has been tested to the Board’s satisfaction, the Board may grant a licence or a provisional licence upon such terms and conditions as it considers necessary”.

The definition of pipeline in the Act, combined with subsection 25(1) and subsection 25(2), creates a situation which places totally unnecessary reporting and review requirements, not only on the gas distributor, but also on this Board. These requirements do not exist in any other jurisdiction in this country.

In EGNB's recent construction application, the gas distributor applied for approval from the Board for the extra high and high pressure pipe required to serve the communities of Moncton, Riverview, Dieppe, Fredericton, Oromocto, Saint John and St. George. This extra high and high pressure pipe was to be laid during the year 2000 construction period. The gas distributor also applied for a permit to construct the "infill" with intermediate pressure pipe in these communities over a twenty year period. There is no question that the high and extra high pressure pipe should be treated in accordance with subsections 25(1) and (2).

However, it is the Board's opinion that the intermediate pressure pipe should not be subject to this section. As the Legislation is presently written, the gas distributor will have to report to the Board as often as each day during construction period. For example, it would report today that it has laid 500 meters of intermediate pressure pipe along Canterbury Drive in the City of Fredericton. The gas distributor would then return the next day and test this pipe and report to the Board. Then the Board would issue a separate license to operate that 500 meters of pipeline. To the best of the Board's knowledge, that kind of reporting and licensing is not required for distribution companies in any other jurisdiction in Canada and most likely not in North America. The Board believes that the Act and regulations set forth a comprehensive scheme to ensure the safety of all pipe which the gas distributor intends to lay in this province. The Board believes that the provisions of section 25

should not apply to intermediate pressure pipe. The Board has safety inspectors on staff to ensure that the Act and regulations are complied with by the gas distributor in the laying of such pipe.

The Board requests that the legislation be amended so that the provisions of subsections 25 (1) and (2) and any other sections which impose unnecessary or onerous reporting or other requirements do not apply to any pipe with a maximum operating pressure under 60 psi (414 Kpa) which would remove the detailed reporting requirements for intermediate pressure pipe or “infill”.

DATED AT THE CITY OF SAINT JOHN, NB this ____ day of _____, 2000.

____
David C. Nicholson, Chairman

____
Léonard Larocque, Commissioner

____
R. J. Lutes, Commissioner

____
Robert Richardson, Commissioner

____
Monika M. L. Zauhar, Commissioner