

MANITOBA | **Order No. 142/05**
THE PUBLIC UTILITIES BOARD ACT | **OCTOBER 27, 2005**

Before: Graham F. J. Lane, B. A., C.A., Chairman
Monica Girouard, C.G.A., Member
Mario J. Santos, B.A., LL.B., Member

**AN APPLICATION BY CENTRA GAS MANITOBA INC. FOR AN
INTERIM EX-PARTE ORDER APPROVING PRIMARY GAS SALES
RATES EFFECTIVE FOR ALL GAS CONSUMED ON AND AFTER
NOVEMBER 1, 2005**

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1.0 EXECUTIVE SUMMARY

In response to Centra Gas Manitoba Inc.'s (Centra) application for interim ex parte approval of amended Primary Gas Rates, the Public Utilities Board (the Board) approves increases by customer class as follows:

Customer Class	Increase
SGS – residential	6.1% to 6.8%
SGS – other	12.4% to 13.8%
LGS	13.3% to 16.0%
HVF	15.4% to 17.3%
Co-op	16.2% to 16.6%
Mainline	16.5% to 17.7%
Interruptible	16.7% to 18.4%

For reasons related to hedging and gas previously acquired at lower prices and placed in storage, none of the increases compare to Centra's recent western supply price of \$12.671/GJ, that being a 44% increase over the August 1, 2005 price.

The rate increases approved, which are to take effect November 1, 2005 are as applied for by Centra with respect to the residential customers within the SGS class. Centra proposed rate increases be restrained for all customer classes in recognition of extraordinarily high commodity prices following natural gas supply problems in the United States as a result of recent hurricanes.

The Board approves Centra's application only with respect to residential customers, and provides relief out of concern for the ability of residential customers, particularly low-income families, to adjust to much higher heating costs this winter.

With respect to Centra's other customers, both those within the SGS class and all other customer classes, the Board rejects Centra's proposal and directs the implementation of rates reflective of Centra's actual cost experience pursuant to a full application of the Board-approved Rate Setting Methodology (RSM). Non-residential customers, particularly commercial and industrial customers, are better able to absorb input cost increases.

For commercial enterprises utility expenses are deductible from income in the determination of taxable income, and a general principle of business is the matching of costs and revenues by fiscal period.

And, while non-residential customers receiving primary gas from Centra will not benefit from the deferral of gas costs provided through this Order, as system-gas customers they are beneficiaries of Centra's hedging and storage actions just as are residential customers. Hedging and gas storage activities have and are expected to considerably reduce costs and rates through this heating season.

By recent Board Order 135/05, the Board suggested Centra defer a portion of the cost of gas incurred with respect to residential customers and recommended Centra propose lower rates than otherwise be the case for November 1, 2005. The concept advanced was based on the premise that residential customers required time to prepare themselves for higher natural gas prices, so as to facilitate measures to improve the heat retention and efficiency of residences. While the RSM remains in place for all customers, with respect to residential customers the full rate effect arising out of the RSM is amended. In essence, only half of the otherwise rate increase impact is to be applied to residential customers.

The Board acknowledges the risks associated with deferring commodity costs from full reflection in rates. If market prices either do not fall or other means are not found to address the deferral of costs now directed, these costs will have to be taken into account in future rate setting, exacerbating what may be an already difficult pricing environment.

Finally, the Board recognizes that restraining rate increases for residential customers will not benefit those customers contracting primary gas through fixed term and price contracts with natural gas brokers. Approximately 80% of Centra's customers depend on Centra-purchased primary gas; the remainder rely on brokers. All customers will benefit from improvements in heating efficiency, as reduced consumption means lower bills.

2.0 BACKGROUND

The five components of Centra's natural gas bill are:

- Primary Gas Rates;
- Supplemental Gas Rates;
- Transportation (to Centra) Rates,
- Distribution (to Customer) Rates; and
- Basic Monthly Charges.

The RSM provides for Primary Gas Rates to be set quarterly on February 1, May 1, August 1 and November 1 of each year. This Board Order sets Primary Gas Rates effective November 1, 2005 pursuant to the RSM.

Quarterly rate setting reflect updated 12-month forward market prices for natural gas, with the forward price being weighted to take into account the cost of gas in storage. In addition to the Primary Gas Base Rate, a Primary Gas Rate Rider (Rider) is attached to the rate concurrent with the Primary Gas Rate change. The Rider is designed to distribute the projected balance in the Primary Gas Purchase Gas Variance Account (PGVA), as at the end of each quarter, over customer bills for the next twelve months of normalized gas usage volumes.

The current RSM involves Centra:

- a) Basing its applications for Primary Gas Rate changes on a twelve-month forward price strip exercised during the first week of the month preceding the commencement of the following gas quarter;
- b) Filing applications on a timely basis on an interim ex parte basis; and
- c) Issuing a press release and a "bill stuffer" communicating the reasons for rate changes as approved by the Board. Centra will notify customers of the rate changes arising out of this Order through a newsletter, *Energy Matters*, and by a Press Release.

Prior to this Order, residential rates had risen by approximately 13% in the last two quarterly settings. This Order will result in winter 2005/06 residential heating rates being approximately 20% more expensive than the residential billed rate at the end of the 2004/05 heating season. The accumulated increase would have been over 30% except for the rate smoothing directed by this Order.

In December 1999, primary gas commodity prices were \$3.00/GJ, and the average annual heating bill for a residential customer was estimated to at \$840. Five years later, the primary gas commodity price had reached \$7.03/GJ and the average residential heating bill \$1,298/year. Today's current market prices of \$12.67/GJ would translate into an average residential heating bill approaching \$1,800/year excepting for the effects from hedging, gas storage and, through this Order, rate smoothing – the combination of which is expected to reduce the \$1,800/year to \$1,358/year given normal weather. These are extraordinary increases matching or exceeding those incurred for gasoline, diesel and propane. Only electricity among energy sources has seen price increases over the past six years of at or below the rate of increase in the Consumer Price Index (Manitoba Hydro's electricity rates have increased by less than the rate of inflation over this period).

Natural gas prices, similar to the situation with coal, uranium, petroleum, gasoline, diesel, fuel oil and propane are of concern to all, though low-income residential customers, in particular, have more difficulty managing the expense increases.

3.0 APPLICATION

On October 21, 2005, Centra applied for interim ex parte (IEP) approval of Primary Gas Rates and a Rate Rider, to be effective November 1, 2005.

Centra proposed rates based on the October 12, 2005 forward price strip for the commodity, applying for the following increases by customer class for November 1, 2005:

Customer Class	Increase Based on Standard RSM	Centra Proposed Increase
SGS (includes residential)	12.4% to 13.8%	6.1% to 6.8%
LGS	13.3% to 16.0%	6.6% to 7.9%
HVF	15.4% to 17.3%	7.6% to 8.6%
Co-op	16.2% to 16.6%	8.0% to 8.2%
Mainline	16.5% to 17.7%	8.1% to 8.7%
Interruptible	16.7% to 18.4%	8.3% to 9.1%

Centra's proposal for residential consumers, which is accepted by this Order, provides for an average increase of 6.3%, or \$81 over a year. If the full increase pursuant to a complete application of the RSM was implemented, the increase would be approximately 12.9%, or \$164, twice that proposed. Under Centra's proposal, all customers receiving system-gas would have received reduced increases, even non-residential customers.

The RSM recommends a Base Primary Gas Rate as of November 1, 2005 of \$0.3506 m³, 20% above the rate that took effect August 1, 2005 of \$0.2916/m³. The RSM derived rate would have been considerably higher excepting for Centra's prior hedging and the gas maintained in storage for withdrawal during the winter season, which was acquired at considerably lower prices.

Recognizing the presence of extraordinarily high natural gas commodity prices, Centra proposed to limit the Billed Primary Gas rates to \$0.3207/m³ - that being 10% higher than August 1, 2005's rate but 10% lower than results from the full application of the RSM.

While developed pursuant to the RSM, the RSM based rate need not necessarily be employed though the recent practice has been to do exactly that.

Noting that market natural gas prices are at the highest levels on record, Centra submitted that phasing in the increase required to reach the RSM determined Base Rate would be appropriate. Centra cited the recommendation in Order 135/05 that it consider rate smoothing. Centra supported its proposal by providing a table disclosing the RSM factors and adjusting the resultant Weighted Gas Cost to provide for half the rate increase otherwise required. The RSM was followed, but the result adjusted.

Component	RSM Based Rates November 1, 2005	Centra's Application November 1, 2005
Date of Forward Price Strip	October 12, 2005	October 12, 2005
12 Month Forward Price	\$ 12.6710/GJ	
Estimated Price Management Impact	(3.0490/GJ)	
Western Supply Price	9.6220/GJ	
Storage Gas Price	7.9250/GJ	
Weighted Gas Cost	9.3140/GJ	\$ 8.5230/GJ
Rate per cubic meter	0.35210/m ³	0.32216m ³
Base Primary Rate with fuel, O/H	0.36178/m ³	0.33184/m ³
PGVA Rider (\$/m ³)	(0.01130m ³)	(0.01130m ³)
Primary Gas reconciliation Rider	0.00018/m ³	0.00018/m ³
Total Billed Rate	0.35066/m ³	0.32072/m ³

Centra advised that the PGVA Rider and the Primary Gas Reconciliation Rider would remain unchanged, but by adjusting the Weighted Gas Cost, the Primary Gas Billed Rate would be lower than the Total Billed Rate, under the standard RSM.

Centra proposed the difference that was expected to develop between the selected \$8.523/GJ Weighted Gas Cost and actual Primary Gas Costs be accumulated in the Primary Gas PGVA. The PGVA balance, projected to be owing to Centra by customers, will be higher than would be the case if the RSM-derived rate was used.

With respect to February 1, 2006 rates, February 1 being the next quarterly rate setting, rates will then depend upon:

- a) futures contract for 12 months commencing February 1, 2006;
- b) revised hedging impacts that will become further known as prices settle from month to month and as forecast for a further 3 months;
- c) weather (which impacts usage);
- d) PGVA balances; and
- e) a decision as to whether further cost deferrals and rate smoothing will take place.

The following table provides the cost components of Centra's Primary Gas Rates for the quarter commencing November 1, 2005, as compared to the last quarter.

Component	Existing Rates August 1, 2005	Standard RSM Rates November 1, 2005
Date of Forward Price Strip	June 20, 2005	October 12, 2005
12 Month Forward Price	\$ 8.7930/GJ	\$ 12.6710/GJ
Estimated Price Management Impact	(0.5180/GJ)	(3.0490/GJ)
Western Supply Price	8.2750/GJ	9.6220/GJ
Storage Gas Price	6.5210/GJ	7.9250/GJ
Weighed Gas Cost	7.9570/GJ	9.3140/GJ
Rate per cubic meter	0.30080/m ³	0.35210/m ³
Base Primary Rate with fuel, O/H	0.30798/m ³	0.36178/m ³
PGVA Rider (\$/m ³)	(0.01660/m ³)	(0.01130m ³)
Primary Gas reconciliation Rider	0.00018/m ³	0.00018/m ³
Total Billed Rate	0.29156/m ³	0.35066/m ³

Factors impacting on the Primary Gas Rate include:

- (a) The western supply price of \$12.671/GJ, a 44% increase over the August 1, 2005 price, which reflects experience pursuant to Centra's current gas supply contract with Nexen Marketing;
- (b) An estimated AECO/Empress basis differential of \$0.1475/GJ from November 2005 to March 2006, \$0.1275/GJ for April to June 2006, and \$0.1300/GJ for July to October 2006;
- (c) Nova to AECO toll of \$0.1509/GJ effective November 1, 2005 to October 2006;
- (d) The estimated mark-to-market price management result of \$3.049/GJ, by Centra's derivative hedging through the placement of cashless collars with \$0.50 out of the money upper strike prices on volumes of approximately 27.0 million GJ. The impact of these transactions, carried out to mitigate price volatility, is an estimated and projected savings to Centra's customers of \$119.0 million from what otherwise would be the cost of gas;
- (e) The cost of gas in storage, projected at \$7.925/GJ (62% of the western supply price), which reflects the forecast cost for the 2005/06-gas withdrawal from storage. The withdrawal covers the period commencing November 1, 2005, and ending on March 31, 2006 and, again, represents cost of gas at much lower prices than current market prices;
- (f) The estimated October 31, 2005 Primary Gas PGVA balance owing to customers is \$13,944,417 resulting in a rate rider of \$.01130 per cubic metre (the approved August 1, 2005 Primary Gas billed rate included a rate rider reducing the billed rate by \$0.01660 per cubic metre to account for the estimated Primary Gas PGVA); and
- (g) A primary Gas Reconciliation Rider, effective from August 1, 2005 to April 30, 2006 to recover the delayed increase in Primary Gas Base Rate overhead component (from February 1 to July 31, 2005). Thus, the November 1, 2005 Primary Gas unit billed rate is \$0.01112 less than the unit base rate.

4.0 COMMENTS FROM INTERVENERS

On receipt of Centra's application, and noting a proposed variation of the application of the effects arising from the RSM, the Board shared the application with Interveners to the recently concluded Centra GRA, as well with all licensed gas Brokers in the Province.

The Board received comments from: Energy Savings (Manitoba) Corp; Coral Energy Canada Inc.; ECNG Limited Partnership and, Direct Energy Marketing Limited / Municipal Gas (Direct).

Each of the responses opposed an exception to the RSM, the deferral of gas costs and the smoothing of rates. Comments expresses included concerns that market prices would not fall making cost deferrals problematic for future rate setting, a perceived need for consumers to realize the full cost of gas and a concern that the competitive market place would be affected negatively.

Direct's submission was reflective of the views of all the brokers, and opined:

a substantive change to the RSM should not take place through a routine quarterly rate setting process;

deferring costs and smoothing rates "discards the key principles of price transparency and market responsiveness underpinning the Board's RSM;

deferral does not lower ultimate costs, prices may rise making later collection more difficult;

false price signals are provided to customers by rate smoothing – reducing the incentive to undertake DSM for consumption reduction; and

rate smoothing by Centra risks the efficacy of the competitive retail market, and may reduce potentially cost-effective choices now available to consumers.

Direct acknowledged that higher natural gas prices will pose hardship for low-income consumers, and suggested that the Board should not reduce and smooth rates but recommend

to government the provision of income supports and the further development of heating efficiency programs. Direct suggested that any proposed change to the RSM should occur through a public hearing that could occur prior to the February 1, 2006 quarterly primary gas rate setting.

5.0 BOARD FINDINGS

The application of full effects arising out of the RSM at a time of extraordinarily high natural gas prices would have a deleterious affect on all residential customers using Centra purchased gas.

Commercial non-residential customers may have the opportunity to pass on input cost increases to customers; the ability to deduct utility costs from taxable income; a capital base sufficient to accept the challenge of higher energy prices; and a preference for matching costs and revenues in the same fiscal period. Residential customers, particularly low-income and fixed-income customers, have less of an ability to meet the challenges higher natural gas heating costs bring.

The Board has noted an increasingly high level of service disconnection, delinquency and bad debts amongst the residential customers, and space heat in Manitoba is a necessity not a luxury. Appropriate space heat is not a matter of assurance of comfort, but also of health. And, not all homes are properly insulated and have efficient furnaces.

The Board supports Centra in its efforts to defer some of the impact of higher natural gas prices on residential customers, particularly those of low and fixed incomes. The avoidance of rate shock for consumers is a normal regulatory practice, followed in fields as diverse as electricity, motor vehicle insurance and water and sewer utilities.

The full application of the effects from the Board approved RSM is a sound concept, that is, if rates change within reasonable bounds. But the 44% price increase in the supply cost

reflected in this Order, and the actual market prices at the date of issuance, are such that the situation cannot be considered normal. Residential customers have already had their billed rates climb by 11% since the last heating season, another 13% jump at this time when service disconnection are already problematic is not reasonable. Time is required to allow residential customers to undertake consumption-reduction DSM initiatives, and they should avail themselves of such programs as now and may exist to make their homes more energy efficient.

As to non-residential customers, the Board holds to the full application of the effects arising out of the RSM. Appreciating the comments of the Interveners, the Board will not defer costs and smooth rates for other than for residential customers. By taking this approach, the amount of cost deferrals will be kept to much lower levels than would otherwise be the case. The Board is very cognizant and mindful of the risk that prices may not fall, or may fall by too small an amount to allow the deferral of costs to be easily managed.

Finally, with respect to the impact of the limited cost and rate deferrals directed by this Order, the Board acknowledges that it may have a negative impact on the affairs of the natural gas brokers selling primary gas supply on a fixed price fixed term basis. In the conflict of principles and objectives, the Board considers the public interest to lie in providing modest protection to residential customers, for a minimum of three months.

The Board hopes that during this period many homeowners will avail themselves of the opportunity to better insulate and take steps for greater energy efficiency. As matters now stand, there could be a significant increase for February 1, 2005 primary rates. Given the extraordinary market price situation and the current deferral of only part of one customer class, the Board will direct that Centra accrue interest on the PGVA related to the deferral at the prime lending rate of a major Canadian chartered bank.

In conclusion, the Board finds that Centra's proposal for a Primary Gas rate change with respect to residential customers properly reflects the current circumstances. Accordingly, the

Board will approve the requested change in Primary Gas Billed Rates as such apply to residential customers as applied for by Centra, to be effective November 1, 2005.

The cost of storage gas, impacts of price management transactions, and the disposition of deferral account balances will be reviewed by the Board at Centra's General Rate Application ("GRA") hearing, which is currently anticipated to proceed in the late spring of 2006.

6.0 BE IT ORDERED THAT:

1. Centra's application for a Primary Gas Billed Rate of \$0.32072/m³ to be effective for all gas consumed on and after November 1, 2005, BE AND IS HEREBY APPROVED on an interim basis for residential customers within the SGS class;
2. For all other customers, including non-residential customers within the SGS class, the full application of the RSM is to be maintained with the rates derived therefrom to be applicable and to be filed by Centra with the Board;
3. That the difference to develop between the selected \$8.523/GJ Weighted Gas Cost and actual Primary Gas Costs for residential customers be accumulated in a separate Primary Gas PGVA bearing annual interest at the prime rate offered by the Royal Bank of Canada, as such may be amended from time to time; and
4. This Interim Order shall be in full force and effect until confirmed or otherwise dealt with by a future Order of the Board.

THE PUBLIC UTILITIES BOARD

“Graham F. J. Lane, C.A.”

Chairman

“G. Gaudreau, C.M.A.”

Secretary

Certified a true copy of
Board Order No. 142/05 issued by
The Public Utilities Board

Secretary