M A N I T O B A	)	**Order No. 170/09**
	)	
THE PUBLIC UTILITIES BOARD ACT	)	**December 21, 2009**

BEFORE: Graham Lane, CA, Chairman
Leonard Evans, LLD, Member
Monica Girouard, CGA, Member

INTERIM REVISIONS: CENTRA GAS MANITOBA INC.'S DERIVATIVE HEDGING POLICY FOR PRIMARY GAS

EXECUTIVE SUMMARY

By this Order, the Public Utilities Board (Board) directs a phase-out of Centra Gas Manitoba Inc.'s (Centra) hedging of Primary gas supply for consumers now receiving "system gas" from Centra. The directives in this Order are in accordance with the prior findings of the Board and are also consistent with the submissions of a major Intervener, representative of consumers, in Centra applications.

BACKGROUND:

On October 9, 2009, Centra filed, for approval, its proposed Derivatives Hedging Policy and Derivatives Hedging Operating Principles and Procedures with the Board.

In addition to the Board's written questions to Centra, the Board also circulated Centra's filing to Interveners (from prior Centra applications) seeking comments. In turn, Centra provided its responses to both the Board's questions and Intervener comments.

APPLICATION:

Centra's proposed revisions to its Policy and the Procedures reflect an intended decrease in the use of derivative hedges, to be accomplished by the placement of hedges on 75% of eligible volumes rather than up to 100% of eligible volumes (as previously approved).

Eligible volumes are the volumes of natural gas that Centra's customers would collectively consume in the warmest year on record. Centra notes that 75% of eligible volumes represents approximately 50% of the collective volumes expected to be consumed in a year with 'normal weather'.

Centra submits that approval of its recommended Policy revision would provide a more balanced approach, than the current approach towards price protection and the risk of gas cost additions brought about due to hedging.

If the application is approved, customers on Centra's quarterly Primary Gas rate service will have exposure to future gas price increases capped for up to a year and a half on the portion of volumes that are hedged and, as a result, those customers will still enjoy a measure of protection from unanticipated and potentially sharp market price increases, albeit to a lesser degree than is and was afforded by the prior hedging of up to 100% of eligible volumes.

In opposition to the position of CAC/MSOS (Consumers' Association of Canada (Manitoba) Inc. and Manitoba Society of Seniors), which seeks a cessation of hedging for quarterly set variably priced system gas, Centra has not requested approval to discontinue hedging altogether. Centra maintains there are rate volatility reduction benefits that the proposed Policy would provide to consumers, and which consumers value.

Centra promises to continue to monitor and assess its derivatives hedging approach and to consider further changes to the Policy, as circumstances may warrant.

Centra's proposed changes to its Procedures related to hedging has responsibility transferred from its Treasury function to its Corporate Risk Management function, to reflect a structural reorganization that took place in March 2009. Centra advises that the closer association of Credit Risk Management to its Corporate Risk Management Department assists in the monitoring and addressing the heightened risk profile of credit issues in its business areas.

(Centra is a wholly-owned subsidiary of Manitoba Hydro, and operates within an integrated Manitoba Hydro organizational structure. Centra has no staff, and relies on Manitoba Hydro staff to operate the utility. Costs are allocated to Centra from Manitoba Hydro in accordance with well-developed cost allocation formulae.)

INTERVENERS' POSITION:

The only intervener to provide comments on Centra's current request was CAC/MSOS.

CAC/MSOS' position continues (in past Centra proceedings, this intervener has, in recent years, consistently sought an end to Centra's hedging) to be that Centra should discontinue its Hedging Program. CAC/MSOS contend that, in the long run, non-hedged system gas represents the lowest cost option for consumers. CAC/MSOS report that Centra's hedging in recent years have resulted in additions to gas costs of $73M in fiscal 2007; $42.5M in fiscal 2008; and, $94.3M in fiscal 2009.

According to CAC/MSOS, consumers looking to take a market view and lock-in Primary gas rates have available fixed rate and term offerings from both a Retail Gas Marketer and from Centra, and, as such, there is no need for Centra to hedge system gas supply for consumers who, in the face of these alternatives, have chosen to stay with Centra's system gas.

CAC/MSOS submit that the reduction in rate volatility brought about by hedging is imperceptible (in the context of the overall average consumer's monthly gas bill), given that the main cause of bill volatility during any quarter is the effect of weather on consumption, and certainly not Centra's hedging.

BOARD FINDINGS:

In Order 128/09 (dated September 16, 2009), the Board noted (and as CAC/MSOS has also documented in its submissions) that Centra's hedging has added significant costs to the overall cost and rates for system Primary Gas in recent years, such that Centra reduced its hedging to 50%, rather than 100%, of eligible volumes. (From the information provided by Centra, Centra hedged 50% of eligible volumes out to April 2010, while, for the gas months of May 2010 to October 2010, Centra has already hedged 75% of eligible volumes.)

For Centra to now advance a proposal that would reduce and limit its hedging to 75% of eligible volumes, from ‘up to 100%’, without supporting detailed analysis, appears curious. Put another way, the Board questions why 75% is now preferred by Centra, rather than the previous 50% of eligible volumes that were hedged until April 2010.

The currently approved Policy permits hedging ‘up to 100%’ of eligible volumes, so the Board considers the requested decline to 75% to technically fall within the existing Policy parameters, and the Board, which in the past has been supportive of a reduction in the percent of eligible volumes hedged, will therefore, approve Centra’s current request but only as the first stage of a transition to the elimination of hedging quarterly priced Primary Gas for system supplied customers.

That said, Centra needs to do more to assure consumers of their ability to enter fixed price and term contracts for Primary Gas from either Centra or a private broker, such that hedging may be entirely discontinued from the quarterly set prices for system gas.

In Order 128/09, the Board leaned towards ending Centra’s hedging program (as suggested by CAC/MSOS), with respect to the quarterly-set ‘system gas’ offering, but was not prepared to act until Centra’s fixed price and rate Primary Gas contract offerings were established for one through five year terms and were regularly offered to Centra’s customer base. The Board encouraged Centra to act much more quickly and comprehensively, to bring forward a full range of fixed price and term contract offerings on a regular basis and with sufficient capacity to allow customers who so elected, to avail themselves of such contracts.

Presently, Centra advises the Board that it is only in its third enrolment period for the Fixed Rate Primary Gas Service (FRPGS), and even if the current offering is fully subscribed, the total number of customers enrolled in Centra’s FRPGS will represent less than 1% of Centra’s total annual system load.

As of November 1, 2009, Centra advises that almost 85% of small volume customers remain on the default supply option, i.e. quarterly set Primary Gas. Centra indicates that the FRPGS is not yet mature enough to support a dramatic alteration of the hedging approach employed for quarterly Primary Gas purchases at this time

Centra's quarterly Primary Gas service has several other non-hedging components that restrain rate and bill volatility for customers not selecting Centra's FRPGS. These include the quarterly refreshing of the Primary Gas rate, the impact of gas purchased and placed in storage during the summer months for withdrawal in the winter, and the availability of Centra's equal monthly payment option.

Centra's promise to make FRPGS more widely available to consumers indicates the time is right to signal customers that the continued hedging of quarterly system gas will cease.

Therefore, to ensure existing quarterly supplied customers have the time and opportunity to be aware of an intended major change in hedging practices, and to be educated as to the options available to them to secure fixed price and term Primary Gas from Retail Brokers or from Centra, the Board will direct Centra to phase out its hedging of quarterly priced system supply.

Unless persuaded otherwise through an application to review and vary this Order, the Board will direct the phase-out to occur in three stages, commencing with this Order.

For the next three gas months' volumes to be hedged, (i.e. November and December 2010 and January 2011), Centra's requested revisions to its Policy and Procedures to hedge a maximum of 75% will be approved. Thereafter, the hedges for following three months (i.e. February, March and April 2011) are not to exceed 50% of eligible volumes. And, for the next three months thereafter (i.e. May, June and July 2011), hedges are not to exceed 25% of eligible volumes.

Commencing with the gas month of August 2011 and following, there is to be no hedging for the quarterly set Primary Gas sold to system customers.

The Board realizes that for the gas months February, March and April 2010 Centra has already hedged 50% of eligible volumes, and that for the gas months May, June, July, August, September and October of 2010, Centra has already placed hedges for 75% of the eligible volumes. This reality supports the Board's directed phase-out of hedging and an increase in Centra's fixed price and term contract offerings, together with a consumer education campaign.

Also as noted in Order 128/09, consumer desire for long-term price certainty supports the continuation of Centra's hedging program for the quarterly system gas offerings until such time as customers are assured of the ability to enter into a fixed price and term contract for Primary Gas with Centra. Other than from Centra, residential consumers seeking longer term rate protection through fixed price and fixed term contracts have only one private retail marketer remaining in the market, a situation that does not represent any significant degree of competition. Accordingly, it is now time for Centra to educate consumers and to take the steps necessary to ensure consumers of their ability to participate in the FRPGS, if they so desire.

The Board will continue to monitor the progress Centra makes towards that goal. In its forthcoming Cost of Gas Application, Centra is to keep the Board current of the steps it has taken, and is taking, to provide wider access to FRPGS.

Board decisions may be appealed in accordance with the provisions of Section 58 of *The Public Utilities Board Act*, or reviewed in accordance with Section 36 of the Board's Rules of Practice and Procedure (Rules). The Board's Rules may be viewed on the Board's website at www.pub.gov.mb.ca.

IT IS THEREFORE ORDERED THAT:

1. Centra's October 9, 2009 request for revision to its Derivatives Hedging Policy for Primary Gas and the Derivatives Hedging Operating Principles and Procedures BE AND IS HEREBY APPROVED, on an interim basis only, for the hedging of 75% of the eligible volumes for the gas months of November 2010, December 2010 and January 2011. Thereafter the hedging of eligible volumes is to be phased out as provided herein with Centra filing its further revised Policy and Procedures every gas quarter.

2. Centra continue to accelerate the steps needed to assure customers of the ability to enter into one through five year fixed price and term contracts for Primary Gas with Centra.

3. This interim Order be confirmed, varied or otherwise dealt with by further Order of the Board through Centra's pending Cost of Gas Application, or as otherwise directed by the Board.

THE PUBLIC UTILITIES BOARD

"GRAHAM LANE, CA"
Chairman

"H. M. SINGH"
Acting Secretary

Certified a true copy of Order No. 170/09
issued by The Public Utilities Board

Acting Secretary