



**ATRIUM  
ECONOMICS**  
CENTERED ON ENERGY

**BEFORE THE PUBLIC UTILITIES BOARD OF MANITOBA**

**CENTRA GAS MANITOBA, INC.**

**2022 COST ALLOCATION REVIEW**

**Written Rebuttal of Atrium Economics**

June 30, 2022



## Table of Contents

<b>I.</b>	<b>BACKGROUND .....</b>	<b>3</b>
<b>II.</b>	<b>SCOPE OF THE ATRIUM REBUTTAL.....</b>	<b>4</b>
<b>III.</b>	<b>THE PUB RECOGNIZED THAT A CONSULTANT WOULD RECOMMEND A CURATED BEST PRACTICE FOR CENTRA .....</b>	<b>5</b>
<b>IV.</b>	<b>CONTRARY TO CAC ASSERTIONS, THE PUB DID NOT APPROVE A PERMANENT COSTING POLICY FOR CENTRA .....</b>	<b>7</b>
	<b>I. THE CAC ATTEMPTS TO REDEFINE COST CAUSATION AND CREATE A POLICY PRONOUNCEMENT .....</b>	<b>7</b>
	<b>II. THE CAC PRODUCES AN OVERLY BROAD AND UNDEFINABLE THEORY OF COST CAUSATION .....</b>	<b>8</b>
<b>V.</b>	<b>THE PROPOSAL TO USE A PEAK &amp; AVERAGE ALLOCATION METHODOLOGY IS NOT A BEST PRACTICE FOR THE CENTRA OPERATIONS, SYSTEM OR COSTS.....</b>	<b>10</b>
<b>VI.</b>	<b>APPLICATION OF THE CAC METHOD IS LESS TRANSPARENT.....</b>	<b>14</b>
<b>VII.</b>	<b>IT IS A COMMONLY ACCEPTED REGULATORY PRACTICE TO DIRECTLY ASSIGN COSTS BASED ON NORMAL UTILITY OPERATIONS .....</b>	<b>14</b>
<b>VIII.</b>	<b>DIRECT COST ASSIGNMENT IS THE MOST ACCURATE DETERMINATION OF COST RESPONSIBILITY.....</b>	<b>15</b>
<b>IX.</b>	<b>CONCLUDING REMARKS.....</b>	<b>17</b>
	<b>APPENDIX A .....</b>	<b>18</b>



## I. BACKGROUND

On June 15, 2021, Centra Gas Manitoba, Inc. (“Centra”) filed an Application in compliance with the Public Utilities Board of Manitoba (“PUB”) Order No. 152/19 which was issued in response to Centra’s 2019/20 General Rate Application (“GRA”). As part of that GRA, the PUB required Centra to file a review of its Cost of Service methodology.<sup>1</sup>

On January 29, 2020, Centra informed the PUB that, among other things, it was in the process of completing the search for an independent consultant to assist in the preparation of a thorough cost of service study. For this and other reasons Centra requested an extension of the filing schedule. In its Findings granting the Centra requests, the PUB deemed it appropriate to insert its thoughts on the importance of an independent consultant.

“The Board expects that the independent expert will be in a position to provide a variety of alternative cost of service study methodology options, each alternative supported by reasons, such that Centra and other Parties will be able to focus their recommendations on the **best practices for Manitoba’s specific circumstances**”.<sup>2</sup> (*emphasis added*)

After the receipt of this order, Atrium Economics (“Atrium”) was retained.

On May 20, 2021, Atrium provided the results of the Cost of Service Methodology Review (“Review”) to Centra. The Review became Appendix 1 to the Centra Application of June 15, 2021. In the Review Atrium made specific recommendations regarding the Centra Cost of Service Methodology. The specific recommendations summarized below are explained in detail in the Review. Briefly stated, Atrium recommended that:

- Centra Replace Peak & Average with a Coincident Peak Day Allocation Method
- Centra’s Design Day Peak is the Preferred Method versus Actual Peak Days
- Centra Directly Assign Transmission Plant to the Special Contract Customer
- Centra Refresh the Development of the Customer Component of Distribution Mains
- Centra Consider an Alternative Approach to the Allocation of Upstream Capacity Resources

On June 8, 2021, Intervenors and Interested Parties filed Pre-Filed Testimony with the PUB. Testimony was filed on behalf of the Consumers’ Association of Canada (Manitoba Inc.) (“CAC”),

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<sup>1</sup> Centra shall file an application for a comprehensive review of its cost of service methodology by no later than May 1, 2020. PUB Order 152/19, page 137, ¶129, October 11, 2019.

<sup>2</sup> Order No. 49/20, April 2020, page 8.

Koch Fertilizer Canada, ULC, (“Koch”), and the Industrial Gas Users of Manitoba, (“IGU”). Atrium reviewed the testimony of all the parties. It is Atrium’s conclusion that most of the parties agree with the Atrium recommendations. Furthermore, Atrium has not found anything in the record to date which suggests that its recommendations should not be fully adopted by Centra or approved by the PUB.

## II. SCOPE OF THE ATRIUM REBUTTAL

The scope of the Atrium rebuttal evidence focuses on two primary issues asserted by the CAC. First, Atrium contends that its recommendation for Centra to replace Peak & Average (“P&A”) with a Coincident Peak (“CP”) Day Allocation Method is a well-reasoned, correct, and regulatory sound one and should be accepted despite the objections of the CAC. Second, Atrium asserts that the recommendation to directly assign transmission plant to the Special Contract customer is grounded in sound costing theory. This results in the most correct allocation of costs to this customer class and should be adopted. This rebuttal testimony is limited to a discussion of the issues set out below, and the failure to address each and every issue in each piece of testimony does not imply agreement with the positions taken by any party with respect to other issues.

Atrium will explain its reasoning and rebut the opinions of the CAC in the following format:

- **The PUB recognized that a consultant would recommend a curated best practice for Centra.**
- **Contrary to CAC assertions, the PUB did not approve a permanent costing policy for Centra**
- **The CAC proposal to use a peak & average allocation methodology is not a best practice for the Centra operations, system, or costs.**
- **Application of the CAC method is less transparent.**
- **It is a commonly accepted regulatory practice to directly assign costs based on normal utility operations.**
- **Direct cost assignment is the most accurate determination of cost responsibility**
- **Concluding remarks**

The positions of the various parties filing Pre-Filed Testimony is outlined in Table 1, below. The Table indicates the recommendations made by Atrium in the Review. It also identifies the positions of the parties: that is, whether they support or oppose the Atrium recommendation. As shown in the table, only the CAC takes positions in opposition to the recommendations made by Atrium.



Atrium Recommendation	Party Supports or Does Not Oppose	Party Opposes
Coincident Peak Day Allocation Method	Centra Industrial Gas Users Koch Fertilizer Canada, ULC	Consumers Association of Canada
Centra’s Design Day Peak is the Preferred Method	Centra Industrial Gas Users Koch Fertilizer Canada, ULC	Consumers Association of Canada
Direct Assignment of Transmission Plant to the Special Contract Customer	Centra Industrial Gas Users Koch Fertilizer Canada, ULC	Consumers Association of Canada
Refresh the Development of the Customer Component of Distribution Mains	Centra Industrial Gas Users Koch Fertilizer Canada, ULC Consumers Association of Canada	None Identified
Alternative Approach to the Allocation of Upstream Capacity Resources	Centra Industrial Gas Users Koch Fertilizer Canada, ULC	Consumers Association of Canada

However, CAC offers no evidence that its positions produce outcomes for the rate payer or consumer that are more equitable or in any way more technically or operationally correct than those recommended by Atrium. Rather, CAC simply argues for a cost causation theory for which there is no industry basis or commonly accepted support and a regulatory policy that does for which there is no predicate. The PUB should reject the CAC proposals and accept all the Centra proposals and Atrium recommendations.

### III. THE PUB RECOGNIZED THAT A CONSULTANT WOULD RECOMMEND A CURATED BEST PRACTICE FOR CENTRA

In the opinion of CAC, the Atrium recommendations are not founded on sufficient industry research a point which is not intended to be “critical” of the work but rather to assess the value of the work undertaken. Atrium should have, CAC asserts, undertaken, “very detailed research”<sup>3</sup> to understand the “...history and context of how approved regulatory methodologies came about”.<sup>4</sup> In short, because the Atrium results differ from those desired by the CAC, the analytical methodology employed by Atrium must be flawed. This results-oriented analysis penetrates the CAC testimony.

<sup>3</sup> Evidence Prepared by Darren Rainkie and Kelly Derksen for CAC, page 19, line 8.

<sup>4</sup> Ibid., page 19, line 9-10.



On the one hand, CAC argues that there is a best practice regarding cost causation and that the PUB has determined it for Centra. It asserts that if Atrium would simply conduct more detailed reviews of Canadian utilities, it would unearth various industry standard practices regarding cost allocation and cost causation. Finally, it suggests that these practices and PUB policy would dictate the use of P&A and an undefinable and extremely broad definition of cost causation.

However, CAC recognizes that there is no single best practice stating that, “There is diversity in COS practice with a range of acceptable methods and no singular industry best practice to rely on for COS decisions”.<sup>5</sup> Later, the CAC expands on the lack of single accepted methodology:

...“it is clear that there is both diversity in practice and a range of acceptable COS methodologies in Canada. It also follows that there is no singular industry best practice that the PUB can rely on to resolve the in-scope issues that are before for it in this proceeding and make COS decisions”.<sup>6</sup>

It is clear that the PUB is of the opinion that there is no industry standard, or no methodology set in stone such that Centra is not free to implement a change in method as a result of the recommendations from Atrium. For example, when ordering Centra to file its cost study, the PUB instructed Centra not to categorically adopt an industry standard but to review options. This is clearly not the directive that the PUB would provide if no methodology changes were permitted.

In its specific directions to Centra, the PUB stated:

The Board expects that the independent expert will be in a position to provide a variety of alternative cost of service study methodology options, each alternative supported by reasons, such that Centra and other Parties will be able to focus their recommendations ***on the best practices for Manitoba’s specific circumstances.***<sup>7</sup> (*emphasis added*)

As a consequence of their engagement, and consistent with the directive of the PUB, Atrium identified a best practice for Centra based on their system operations and associated appropriate determinations of cost responsibility using industry accepted cost causation norms and theoretical methods.

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<sup>5</sup> Ibid., p 20, line 25-26.

<sup>6</sup> Ibid, page 21, line 15-18

<sup>7</sup> Order No. 49/20, April 2, 2020, page 8.

## IV. CONTRARY TO CAC ASSERTIONS, THE PUB DID NOT APPROVE A PERMANENT COSTING POLICY FOR CENTRA

The PUB should not be persuaded by the opinions that there is a long-standing policy requirement to use P&A and a theoretical and undefinable cost causation theory. The CAC asserts that the PUB has a long-established policy that requires gas utilities to use P&A. Two key points of the CAC position are:

- i. “Cost causation should continue to be the primary driver of COS policy and be given the most weight in selection of cost allocation methodologies; and ...
- ii. While cost causation is the primary driver, it should not be a sole consideration, as it is impractical to remove all other ratemaking objectives as they are inherently an important element of developing a cohesive and workable COS framework”.<sup>8</sup>

Each of these points will be discussed in turn.

- i. The CAC Attempts to Redefine Cost Causation and Create a Policy Pronouncement

CAC first defines a new concept of cost causation and claims it as a policy pronouncement. The CAC selectively quotes from a previous PUB Order in an attempt to justify its position.

“The Board further expects that the primary driver will be cost causation with due regard to Centra's current operations in the Manitoba market, direct purchase activities, storage arrangements, risk management activities, ***weather and use patterns*** for each specific customer class and ***all other relevant issues***.”<sup>9</sup>***(Emphasis added)***

However, the language cited from the PUB order is taken out of context. It is in fact originally from PUB Order 49/95, and it was cited in Order 107/96 by the PUB in a discussion of the historical background of cost of service and rate design proceeding for Centra. It was not cited in any finding or ordering language in the Order. In other words, it is irrelevant to the specific findings in Order 107/96.

However, a more detailed review of Order 49/95 provides insight into matters that are relevant to this proceeding. For example:

1. Centra submitted a fully allocated Cost Allocation Study as part of the original GRA filing. (See Order at ¶26.1 page 104)

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<sup>8</sup> Rainkie Derksen, page 11, line 15-21

<sup>9</sup> Ibid., page 11, line 30 – 34.

2. CAC/MSOS did not pursue the matter of cost allocation to any great extent. (See Order at ¶126.5, page 105)
3. The Board noted that all parties generally agreed that the cost of service should be reviewed and that the CAC/ MSOS only requested that changes be made upon the detailed completion of cost allocation and rate design. (See Order at ¶126.6 page 106)
4. It was only in the context of ordering a future review that the PUB used the indicated language, not in the context of a finding or policy pronouncement.

ii. The CAC Produces an Overly Broad and Undefinable Theory of Cost Causation

The CAC manufactures a definition of cost causation that is undefined in their testimony and unknown in the industry. They assert that the Commission utilizes a “broad” definition of cost causation citing the PUB in Order 107/96, Pages 26 to 27. However, a review of the Order indicates that the facts are otherwise.

First, CAC selectively quotes the PUB and considers the citations out of context. Second, they read the quotations literally, assuming that there is no nuance or larger meaning to be garnered from the surrounding context. Finally, they make the unsupportable assumption that because something once was determined to be appropriate, it can never be changed. This final point means that regardless of the change in operations, or customer services, or any other matter which may come before the regulator, the die has been cast and the methodologies are set in stone.

Fortunately, the PUB has a different perspective. Indeed, in its Findings in Order No. 107/96 the PUB explained that its findings are flexible and are intended to recognize the contemporary utility operations. In that Order the PUB stated:

“... The Board's expectation is that the principles herein approved will be adaptable to industry changes and that the results produced should be acceptable for some time into the future” (Order 107/96, at ¶13.1 page 26), and

“...cost allocation methodology...must reflect the manner in which the system is **designed as well as the manner in which it is operated**”. (Order 107/96, at ¶13.1 page 26) (*emphasis added*)

Equally important the PUB noted that the docket in question was not solely a cost allocation study proceeding but rather one to determine class revenue requirements, cost allocation and service rates. And the PUB specifically noted that the duration of the use of P&A could be limited. To that end, the PUB noted:

*“This proceeding was not to set rates reflecting the cost allocation methodology results but to approve principles to be included in both the methodology and the rate design structure”.* (Order 107/96, at ¶13.1 page 26); and



“While it is ***difficult to determine the longevity of any methodology***, the Board is satisfied that the peak and average method for allocating demand related costs will remain relevant for some period of time”. (Order 107/96, at ¶13.1 page 27) (***emphasis added***)

It is worth noting that in 107/96 CAC/MSOS submitted its novel theory of cost causation in testimony to that proceeding. However, the PUB did not make a specific finding on the theory. In that proceeding, CAC/MSOS submitted that the purpose of a cost allocation study is to provide the Board a guideline to use in attempting to arrive at fair and reasonable rates. They submitted that cost caused rates do not equate to fair and reasonable rates and that the PUB should not consider fairness and equity in a purely economic sense. CAC/MSOS went on to state that cost causality should be the primary driver of rates, but not the only driver. Non-cost causal factors should be considered and should be considered in the cost allocation stage rather than at the rate design stage.

As part of this theory, CAC/MSOS believed an attempt to institute non cost causal factors at the rate design stage would not be pragmatic and would lead to considerable controversy if a revenue to cost ratio of unity were not applied to all customer classes. CAC/MSOS requested that the Board approve Centra's proposed cost allocation methodology, including the use of the P&A method to determine the demand allocator. While the PUB approved the P&A proposed by Centra, they did not approve the methodology that CAC/MSOS proposed.

Atrium agrees that cost causation should be the primary driver of the cost allocation process and has stated this in its Review and its responses to IRs. However, CAC takes the “broad” cost causation theory much farther than simply giving greater weight to other factors, instead making them equal to or greater than the primary driver of costs. Indeed, no factors can be considered in isolation, and the appropriate weight and order of analysis must be assigned. Atrium did review system usage and operations when evaluating costing to understand how these contributed to cost incurrence in general and to individual customer costs in particular. The result of the review was a determination that new methods were appropriate given the existing utility operations.

As part of its participation in Docket No. 107/96, CAC agreed with the results of the Centra proposal only and only requested that the PUB approve the Centra method. They did not specifically request approval of the CAC “broader” cost causation methodology. Nor did CAC request adoption of a new policy. Nor did the PUB approve one.

CAC also asserts that the PUB should weigh an innumerable future set of assets which may have no cost relationship to the current services at hand and to which CAC has offered no cost relationship. In addition, they suggest that the PUB should abandon the entire concept of the test year and endeavor to match cost responsibility from multiple years to costs from a single year. In the testimony the CAC states:

“The broader definition of cost causation ... should consider and give weight to all of the uses and benefits of assets, including primary and secondary uses and benefits, over a range of years (and not just the test year) and over a range of operating conditions.”<sup>10</sup>

The language of the Order No. 107/96 is straightforward, and the PUB only approved the allocation method and not a “broader” cost causation theory. The Findings language makes it clear that the method was only adopted because of a perceived flexibility and the ability to make future modifications. This clearly suggests that the PUB intended that the was not a permanent method. The CAC reads far too much into this Order.

To adopt the broader definition of cost causation that CAC desires is untenable. To accomplish this, CAC utilizes an inductive analysis of cost causation and allocation to achieve its results whereas Atrium proposes to use a deductive analysis. To achieve the outcome, CAC must paint all costs causation equal for all customer classes; in other words, create the “broad” definition of cost causation. CAC desires an outcome that ignores true cost responsibility, punishes economic efficiency, distorts market signals, and encourages inefficient energy choices. The position is untenable.

## V. THE PROPOSAL TO USE A PEAK & AVERAGE ALLOCATION METHODOLOGY IS NOT A BEST PRACTICE FOR THE CENTRA OPERATIONS, SYSTEM OR COSTS

CAC recommended the PUB retain P&A for the allocation of demand-related transmission and distribution investment, while acknowledging that “[f]rom gas engineering perspective, its appropriate and clear that a peak demand design criterion is utilized when designing a gas distribution system to accommodate the gas demand requirements of the customers served from that system.”<sup>11</sup> CAC asserts, notwithstanding this fact, that cost allocation should also weigh costs with unspecified “primary” and “secondary” benefits.

As mentioned earlier, Atrium, as an independent expert provided Centra with analysis and recommendations for “the best practices for Manitoba’s specific circumstances” in accordance with the PUB directive. A key recommended best practice is the adoption of the CP allocation method. Continued use of the P&A method would not be a best practice for Centra. Our recommended design day allocation method is explained in the Review in Section 4.3.

By definition, a utility’s design day demand is as stable a determinant of planned capacity utilization as you can derive. If it were not a stable demand determinant, the design of a utility’s gas system and supply portfolio would tend to vary and make the installation of facilities and

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<sup>10</sup> Rainkie Derksen, page 13, line 13-16.

<sup>11</sup> Ibid, page 27 line 35-36.

acquisition of supply resources and capacity a much more difficult task. Therefore, use of design day demands provides a more stable basis than any of the other demand allocation factors available based on either actual peak day demand or the averaging of multiple peak days. In Atrium’s experience, there is no better way to capture the true cost causative factors of a gas utility’s operations than to utilize its design day peak requirements within its cost of service studies.<sup>12</sup>

Witness Collins emphasizes the deficiencies of P&A:

“The P&A is not reflective of cost causation. Centra’s system must be sized to meet its design day peak demand. A system designed to meet the average demand could not serve the load on days in which the demand is above the average, which would be almost all the cold winter days. Average demand is obviously not reflective of cost or the basis for the design of the Centra system”.<sup>13</sup>

Atrium has explained that the P&A method encourages inefficient use of the distribution system and penalizes efficient use of the system by high load-factor customers in our Review on pages 4 and 5.

These points are echoed by Witness Collins:

“...the P&A method’s cost allocation formula would unfairly increase the allocation on throughput and punish the higher load factor classes that are responsible for increasing the efficiency of the system. The use of average throughput penalizes customers that exhibit efficient gas consumption (higher load factors). Under-utilization of the system should not be rewarded since it results in higher per unit prices for all customers”.<sup>14</sup>

Atrium has noted that P&A may be correct, in a situation where the facts are different than those present at Centra. Witness Bowman notes this fact:

“It is also important to note that the existing Peak and Average approach is, on occasion, used in the allocation of gas utility costs, where facts differ from CGM’s. In particular, the situations in which it is used are typically different than the gas distribution nature of CGM’s operation. Atrium gives one such example in response to CAC/Atrium I-2f, where a gas utility is described as having multiple

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<sup>12</sup> IR response CAC/ATRIUM I-3k

<sup>13</sup> Testimony of Brian C. Collins for Koch, page 4, line 11 – 15.

<sup>14</sup> Collins, page 3, line 20 – page 4, line 2.

trading points, and costs that must be allocated between both sales and transportation customers (a feature that CGM does not have)".<sup>15</sup>

CAC does not provide any examples of a comparable system that utilizes a P&A methodology because of a regulatory finding. They rely solely on a misrepresentation of a previous PUB order.

Since the Atrium analysis operates within the limits of the model defined by the PUB<sup>16</sup> the recommendations stayed true to the tenets of cost allocation theory. Atrium recommends a method that will produce accurate, fair, and equitable results. From a cost perspective there is no undue subsidization either between customers within the same class or across different classes of customers. Despite CAC's casual statement that, "size matters" and the associated assumption that these customers should receive some special benefit, size alone is not a determinant for a customer class. For example, considerations such as the location, type of meter and service, demand characteristics, size, and a variety of other factors are often recognized to properly distribute the total cost of service to and within customer classes.

This concept is also directly related to the concepts of vertical and horizontal equity. The principle of horizontal equity requires that "equals should be treated equally" and vertical equity requires that "unequals should be treated unequally". Specifically, these principles of equity require that where cost of service is equal – rates should be equal and, where costs are different – rates should be different.

Centra relies upon design day demand in the acquisition of its upstream gas supply related capacity resources and in the design of its own transmission and distribution facilities required to service its customers in its 26 service areas connected to TCPL. Importantly, design day demand directly measures the gas demand requirements of the Company's customers which create the need for the Company to acquire resources, build facilities and incur millions of dollars in fixed costs on an ongoing basis. Atrium recommends the use of a coincident peak allocation of transmission plant to the rate classes based on the proportion to their design day peak load requirements.

Further, CAC claims that Atrium summarily dismissed NCP and incorrectly attributed the use of it to Enbridge Gas, which is inaccurate, as shown in Appendix C of our report on pages C-8 through C-9, and C-15 through C-16. The use of the NCP method is discussed in Appendix C to our report for APEX (f/k/a Alta Gas, Inc.) on pages C-1 through C-4, and ATCO Gas North on pages C-5 to C-7. In both cases the use of NCP was employed for the purpose of assigning cost responsibility to seasonal customer classes.

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<sup>15</sup> Testimony of Patrick Bowman for Industrial Gas Users of Manitoba, page 6.

<sup>16</sup> Atrium submits that since the CAC proposed to impose rate mitigation measures in the guise of cost allocation it is imposing rate design in the cost study, a point to be discussed below.

As mentioned in the Atrium Review, the NCP allocation method, which uses the classes' maximum demands on days whenever they occur, is rarely used for gas LDC cost of service studies. The NCP assumes that the cost of distribution facilities should be allocated as though each customer class was served alone regardless of the timing of the maximum class demands. Thus, it allocates capacity costs to all classes of customers regardless of whether or their maximum demands coincide with the system coincident peak. In his seminal treatise on public utility regulation, Professor Bonbright states:

“Economists have been particularly critical of this method as it ignores variations in the timing of the peak demands. In the words of Nobelist W. Arthur Lewis (1949), referring to attempts by rate engineers to offset its obvious informalities by allowances for the different diversity factors of different groups of customers: ‘...no amount of correction can alter the fact that the standing costs of the undertaking are related not to the maximum rate at which the individual customer takes, but to the amount he takes at the time of the station peak.’ (But this sentence should have been amended to include not only the station peak, but the distribution system peak, which may be an even more critical factor.)”<sup>17</sup>

Professor Bonbright further criticizes the NCP method as follows: “The noncoincident demand method, despite its wide-spread use, is based upon two fallacies and, in fact, is not really a cost analysis at all.”<sup>18</sup> He references another economist, Clair Wilcox:

“First, it involves circular reasoning. The differences in demand that are used as a guide in allocating costs are not independent of differences in rates. ... Second, the method does not make proper allowance for the factor of diversity. The concept of maximum coincident demand for a utility system as a whole is meaningful. The concept of aggregate noncoincident maximum demands of customer classes is not. A company does have to build plant big enough to meet the peak of coincident demand. It does not have to build one big enough to meet the aggregate of noncoincident demands. For such demands, by definition, occur at different times. If a customer’s maximum comes at the same time as the system’s maximum, he may properly be charged with more responsibility for the size of the investment that is required. If it comes at any other time, he should be charged with less.”<sup>19</sup>

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<sup>17</sup> James C. Bonbright, Albert L. Danielsen and David R. Kamerschen, Principles of Public Utility Rates, 1988 Edition, at 496.

<sup>18</sup> *Ibid*, at 461.

<sup>19</sup> Clair Wilcox, William G. Shepard, Public Policies Toward Business, (1975), at 333.

## VI. APPLICATION OF THE CAC METHOD IS LESS TRANSPARENT

Atrium contends that the methodologies advocated by the CAC create improper cost subsidies between classes and distorts the true cost of providing natural gas service for the consumer. To the extent that a regulatory body determines that cost mitigation steps should be taken, it should be managed in the revenue apportionment phase of the process where all parties can observe the changes, evaluate the impacts, and make valid market choices. When cost subsidies are hidden in the cost of service study, true cost causation transparency is lost. This is one of the many issues with the proposals made by the CAC. Because it moves class revenue mitigation into cost allocation, it buries the impacts of the class cross-subsidies making them opaque and blurring the cost impacts to customer classes.

Specifically, under the CAC approach the mitigation step would be reflected in the cost of service study as cost sifting would occur to higher load factor customers. In Order No. 107/96, the PUB noted that the CAC had opined:

“...Non cost causal factors should be considered and **should be considered in the cost allocation** stage rather than at the rate design stage...They submitted that a Board decision incorporating non cost causal factor in the cost allocation would enable all interested parties to know the rules of the game...”.<sup>20</sup> **(emphasis added)**

The PUB went on to note that the CAC:

<sup>21</sup>“... was of the opinion **that an attempt to institute non cost causal factors at the rate design** stage would not be pragmatic and would lead to considerable controversy if a revenue to cost ratio or unity were not applied to all customer classes”. **(Emphasis added)**

By their own admission, the CAC is advocating for a cost mitigation process in a cost of service study, which it recognizes is a part of the rate design process. These non-cost causation factors should be evaluated outside of the scope of a cost service study.

## VII. IT IS A COMMONLY ACCEPTED REGULATORY PRACTICE TO DIRECTLY ASSIGN COSTS BASED ON NORMAL UTILITY OPERATIONS

Atrium reviewed the cost related to providing gas service to the Special Contract customer and, based on the normal daily operations of the system as well as the other matters noted in the

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<sup>20</sup> Order 107/96, ¶ 11.1, page 22.

<sup>21</sup> Ibid, pages 22 to 23.

Review, Atrium recommended that the costs for this service should be directly allocated. CAC opposes the direct allocation of these costs. Among other things, CAC disputes that normal operations are a viable basis for allocating costs. However, CAC concedes that there is a difference between *normal* operating conditions and other situations which preclude service to a customer, “...assets may serve a customer under some conditions, such a (*sic*) normal operating conditions, but may not be able to support the customer (s) under all operating conditions”.<sup>22</sup>

Witness Collins agrees with Atrium, noting “...Atrium is correct in its conclusion that the appropriate cost allocation methodology should be based on normal operations ***not an abnormal or unique emergency situation that may never occur***”.<sup>23</sup> (*emphasis added*).

As was observed in the Review, the normal operations are for the Brandon System to be run isolated from the rest of the system and the high-pressure lines used to service the SC and PS Customers. Among other things, gas to the Special Contract customer must be delivered in an unodorized state. This is a contractual requirement of the service. Consequently, compliance with safety management requires that the line be isolated from those deliveries points that require delivery of gas where safety requirements necessitate odorization. This, among other daily operational considerations, dictates that the normal operations of these facilities are such that they operate in isolation from the rest of the system.

Cost causation principles dictate that a customer or groups of customers that cause the utility to incur costs should be responsible for those costs. If a direct linkage between a utility’s customers and the costs incurred by the utility in serving those customers is established, that cost is deemed a directly assignable cost.

## VIII. DIRECT COST ASSIGNMENT IS THE MOST ACCURATE DETERMINATION OF COST RESPONSIBILITY

In testimony, CAC asserts that costs should be generally allocated rather than directly assigned, stating that, “[u]tility plant is fungible in that the investment can serve different purposes over time and as such is generally allocated rather than directly assigned to customers classes”.<sup>24</sup>

The “fungibility” of gas plant is a novel theory which, to the best of Atrium’s knowledge, has never been asserted or accepted by any regulatory authority. Furthermore, direct assignments best reflect the cost causation characteristics of serving individual customers or groups of customers. Therefore, in performing a COSS, maximizing the amount of plant and expense

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<sup>22</sup> Rainkie Derksen, page 4, line 4 – 6.

<sup>23</sup> Collins, page 8, line 14 – 16

<sup>24</sup> Rainkie Derksen, page 39, line 9-10.

directly assigned to particular customer groups to avoid the need to rely upon other more generalized allocation methods.

Direct assignments are also explicitly advocated by the American Gas Association rate committee:

“An analysis of accounts may indicate specific costs that should be assigned directly to a particular class of service. These costs might include, for example, a lateral gas main built specifically to serve one of a group of industrial customers. Both the plant investment and associated expenses of this lateral should be assigned directly to the industrial class.”<sup>25</sup>

As Atrium notes in our Review, direct cost assignment is the best determinant of cost responsibly when a direct line of cost causation can be established. Witness Collins agrees, citing an Atrium response to an IR which stated:

“Subsidies cannot be the result of a correctly assigned direct cost. When costs are directly assigned, a direct relationship has been determined between cost causation and responsibility for the customer to pay for those costs. In contrast, subsidies can occur when direct assignments of cost are not possible as the determination of appropriate allocation factors is only a best effort to approximate the relationship between cost causation and the allocated result of the cost of service study”.<sup>26</sup>

The normal operations of the Brandon System when delivering gas to the SC and PS services establishes a direct cost causal relationship and is detailed in the Review and highlighted in Appendix A (excerpt from Review).

Atrium has already detailed at length, through its Review and its responses to IRs, ample evidence that direct costs assignment is appropriate. Various intervenors have also filed in support of direct costing where appropriate. For example, Witness Collins notes that the NARUC Gas Distribution Rate Design Manual states, “The assignment of direct cost is straightforward and should not be subject to debate”.<sup>27</sup> Similarly Witness Bowman cites the NARUC manual noting:

“All items that can be directly attributed to a particular service (such as revenues from a specific service or the cost of a high pressure main constructed for a

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<sup>25</sup> Gas Rate Fundamentals Fourth Edition, 1987, American Gas Association, SEGREGATING DIRECTLY ASSIGNABLE COSTS, page 140-141.

<sup>26</sup> *Ibid.*, page 8, line 6 – 13.

<sup>27</sup> Collins, page 7, line 19-20.



particular customer or group of customers) should be segregated and directly assigned to the appropriate customers”.<sup>28</sup>

And then adds,

“Only for costs where causation or responsibility is shared do methods of allocation become necessary”.<sup>29</sup>

Importantly, the direct allocation of costs does not mean that SC and PC avoid the sharing of any jointly caused costs. For example, a review of the allocation factors indicates that among others, the SC and PS services are allocated (e.g., intangible and general plant, corporate overheads, just to name a few). The fact that some costs, or even that most of the costs are identified as direct does not preclude the allocation of all costs if some of those are appropriately identified as allocable to the SC and PS services.

## IX. CONCLUDING REMARKS

CAC first advanced their argument of “broad” cost causation and cost mitigation in Docket No. 107/96. In this proceeding they have asserted that the PUB approved their theory and adopted it as their policy. In fact, the PUB issued a narrow finding on the cost allocation approving the implementation of the requested Centra methodology and did not make a finding as to the theoretical pronouncements enunciated by CAC.

The CAC has not supplied any support or reasoning for its recommendations beyond its belief that its theory should be policy. All other parties in this proceeding support the recommendations made by Atrium. It is noteworthy that no other parties see the policy conflict that CAC raises. Atrium provided an independent review for Centra with specific recommendations, many of which Centra proposed to implement.

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<sup>28</sup> Bowman, page 4.

<sup>29</sup> Bowman, page 4



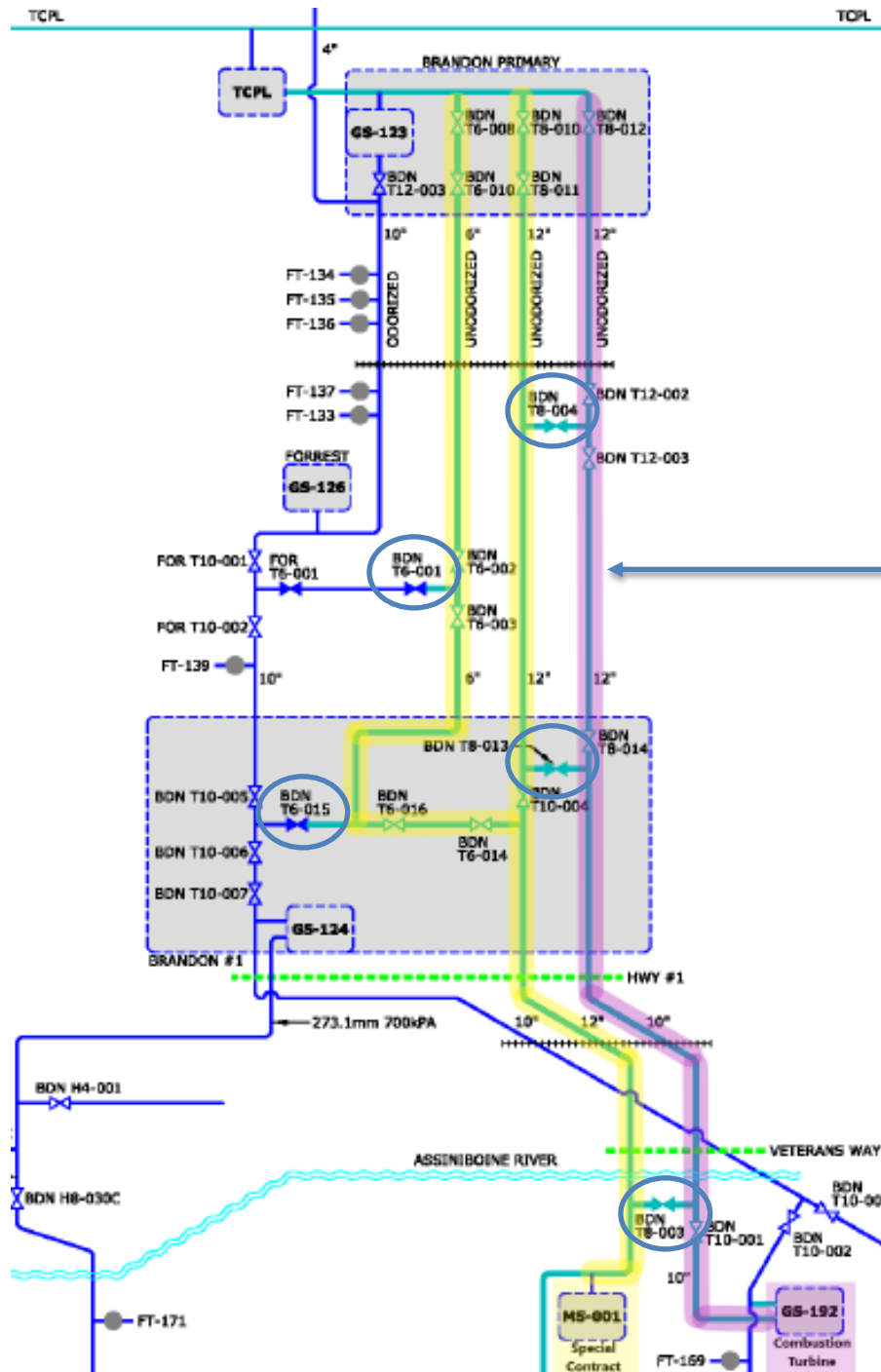
## Appendix A

Atrium recommends that the Special Contract customer receive a direct assignment of the transmission mains that serve its industrial facility. Atrium reviewed the Special Contract customer's contract terms; interrogatories and testimony from Centra's last rate proceeding; details of the special contract customer's service characteristics; physical location of the customer on the Centra transmission system; significant historical load changes; and other relevant information for consideration as we evaluated alternative costing methods. Based on this review we determined the following:

- The transmission pipeline segments are exclusively used to provide service to the Special Contract customer.
- Under normal operating conditions, the transmission lines providing service operate in isolation from the remainder of the transmission system.
- A direct interconnect with TCPL via Centra's Brandon primary gate station serves the entire load requirements of the Special Contract customer's industrial facilities.
- The transmission pipeline segments operate at a higher pressure than most of the rest of the Centra system; the Special Contract customer requires higher pressures to maintain plant operations, having entered into a minimum delivery pressure agreement with the upstream transmission pipeline, TCPL, to promote operational stability.
- The Special Contract customer requires non-odorized gas, which necessitates isolation of the parallel transmission pipelines from which the Special Contract customer receives service and inhibits the active interconnection of these pipeline segments with the broader transmission system.
- The remainder of the Centra transmission system is fully odorized, physically separated by valve stations which remain closed under normal operating conditions and receives only one-way pressure and capacity support in an emergency situation from the transmission pipelines that serve the Special Contract customer.

The following schematic diagram, an excerpt from Centra's system maps, in **Figure 1**, shows the location of the Special Contract customer and one of the two Manitoba Hydro Power Stations, on the Centra transmission system.

Figure 1



Valves BDN T6-001 & BDN T6-015 are normally closed

Valve BDN T8-004 is normally closed

This pipeline is normally dedicated to the CT and does not supply Koch

Valve BDN T8-013 is normally closed

Valve BDN T8-003 is normally closed



As shown in **Figure 1**, gas flows to the Special Contract customer through the Brandon Primary gate station and downstream through a 6” and 12” transmission pipeline to the customer’s industrial facility. Further, the schematic diagram indicates that the valves between the odorized transmission pipeline and the high-pressure 6” transmission line are operating in the closed position. The parallel high-pressure transmission lines are designated as “unodorized”.

A review of this schematic diagram, in addition to the operational information provided by Centra, demonstrates that the gas flowing to the special contract customer is exclusively from the Brandon Primary gate station through the 6” and 12” lines and to the Special Contract customer’s industrial facility. The normal operation of these pipelines has evolved to meet the requirements of the Special Contract customer and, since approximately 2011, they have been dedicated to the purpose of serving the maximum demand, pressure requirements and non-odorized gas supply of the Special Contract customer. It is entirely appropriate to directly assign the cost responsibility for these pipeline facilities to the customer when a nexus between the cost incurrence and the customer can be identified. Therefore, Atrium recommends that the demand-related cost for these transmission mains be directly assigned to the Special Contract customer and no allocation of the broader transmission system capacity.