

NOVA SCOTIA UTILITY AND REVIEW BOARD



IN THE MATTER OF THE GAS DISTRIBUTION ACT

- and -

IN THE MATTER OF AN APPLICATION by **HERITAGE GAS LIMITED** for approval of its Customer Retention Program pursuant to Section 22 of the Gas Distribution Act

BEFORE: Peter W. Gurnham, Q.C., Chair
Roland A. Deveau, Q.C., Vice-Chair

COUNSEL: **HERITAGE GAS LIMITED**
David MacDougall, LL.B.
Sara Mahaney, LL.B.
Michael Johnston, Manager of Regulatory Affairs

CONSUMER ADVOCATE
John Merrick, Q.C.

CANADIAN PROPANE ASSOCIATION
Nancy G. Rubin, Q.C.

KILLAM APARTMENT REIT
Philip Fraser, President and CEO

NOVA SCOTIA DEPARTMENT OF ENERGY
Sean Foreman, LL.B.

BOARD COUNSEL: S. Bruce Outhouse, Q.C.

HEARING DATE: July 4, 2016

FINAL SUBMISSIONS: July 25, 2016

DECISION DATE: September 8, 2016

DECISION: Application approved.

1.0 INTRODUCTION

[1] This Decision is further to a public hearing conducted by the Nova Scotia Utility and Review Board (“Board”) respecting an application filed on March 2, 2016, by Heritage Gas Limited (“Heritage”, “Company”, “Utility”) for approval of its Customer Retention Program (“Application”), pursuant to s. 22 of the *Gas Distribution Act* (“Act”).

[2] The Application includes requests for the following relief:

- a reduction in the existing Base Energy Charge (“BEC”) for Rate Class 1 (“RC1”) commercial customers whose annual consumption is at, or above, 500 GJs/year;
- full suspension of depreciation of its plant-in-service while the reduced BEC is in place; and
- permission to capitalize 50% of its Operating, Maintenance and Administrative (“OM&A”) expenses while the reduced BEC is in place.

[3] Heritage is making its Application due to competitive pricing pressures from other energy commodity products, notably from propane. In its Application, Heritage noted its understanding that many RC1 commercial customers are being offered propane prices which are up to 35% lower than natural gas on an equivalent delivered basis. To the date of Application, over 250 RC1 commercial customers have either switched to propane or are making plans to do so. Heritage submitted that the departure of these customers has significantly impacted Heritage because they account for approximately 350,000 annual GJs and over \$3 million in annual revenue, most having left the system in a relatively short period of time. Further, it said the low price of propane relative to natural gas has significantly reduced the number of commercial customers choosing to convert from oil or propane to natural gas.

[4] The reasons for the Application were explained by Heritage:

Heritage Gas’s goal with these requests is to enable the company to retain existing RC1 commercial customers on its natural gas distribution system and to stay competitive in the

marketplace, which is in the best long-term interests of all of its customers and potential future customers. Recently, due to the relative changes in energy commodity prices, Heritage Gas has been facing intense competitive pressure for commercial customers in its existing RC1 customer class.

Heritage Gas believes granting its requests in this Application is in the public interest as it will aid substantially in retaining a significant portion of its RC1 commercial customers who account for a substantial amount of delivery revenues and throughput of Heritage Gas. Being able to keep these customers in Heritage Gas's system is critical. It will significantly help to ensure the sustainability of the natural gas distribution system and affordability of natural gas as a clean, reliable and safe energy source in the Province of Nova Scotia.

[Exhibit H-1, p. 3]

[5] As part of its Application, Heritage also applied for interim approval, pursuant to Section 21(1A) of the *Act*, to allow Heritage to extend its proposed BEC reduction to RC1 customers on an expedited basis. The Board convened a hearing on March 21, 2016, regarding Heritage's interim approval request. After hearing the evidence of Heritage's witness panel, and submissions from Formal Intervenors, the Board delivered an oral Decision at the hearing approving the Revised Tariffs on an interim basis, effective March 22, 2016. However, the Board deferred to the hearing on the merits the request for interim relief related to the suspension of depreciation of Heritage's plant-in-service, and the proposed 50% capitalization of its OM&A expenses.

[6] The Board issued an Order on March 22, 2016, approving the Revised Tariffs on an interim basis, and setting the matter down for a hearing on the merits commencing Monday, July 4, 2016.

[7] In its Order, the Board directed that its consideration of the Application would be conducted in accordance with the following timetable:

| | |
|--|--------------------------|
| Information Requests (IRs) to Heritage | Thursday, April 7, 2016 |
| Heritage Responses to IRs | Thursday, April 21, 2016 |
| Filing of Intervenor Evidence | Thursday, May 5, 2016 |
| Heritage IRs to Intervenor | Thursday, May 19, 2016 |
| Responses to Heritage IRs | Thursday, June 2, 2016 |
| Heritage Rebuttal Evidence | Thursday, June 16, 2016 |
| Requests to Speak | Wednesday, June 29, 2016 |
| Letters of Comment | Wednesday, June 29, 2016 |
| Opening Statements | Wednesday, June 29, 2016 |
| Hearing Commences | Monday, July 4, 2016 |

[8] A total of six Formal Intervenor responded to the Notice of Hearing including: the Consumer Advocate (“CA”); the Canadian Oil Heat Association – Nova Scotia (“COHA-NS”); the Canadian Propane Association (“CPA”); Killam Apartment REIT (“Killam”); the Nova Scotia Department of Energy (“Province”); and Peter Allen, P.Eng. COHA-NS and Mr. Allen did not participate in the hearing on the merits.

[9] S. Bruce Outhouse, Q.C., acted as Board Counsel.

[10] On June 29, 2016, Heritage and the CA filed a Consensus Proposal. A copy of the Consensus Proposal is attached as Appendix “A” but the principal provisions provide:

1. Reduction in Rate Class 1 commercial customers at or above 500 GJs/year Base Energy Charge (“BEC”) with pricing flexibility approved as described in Heritage Gas Rebuttal Evidence.
2. Depreciation deferral approved as described in Heritage Gas Rebuttal Evidence with the carrying cost to apply of 4% rather than 4.5%.
3. OMA deferral approved as described in Heritage Gas Rebuttal Evidence with the carrying cost to apply of 4% rather than 4.5%.
4. BEC for Rate Class 1 Residential and Small Commercial (<500 GJ/year) customers to be reduced by \$0.50 per GJ for bills issued between November 1, 2016, and April 30, 2017, and from November 1, 2017, to April 30, 2018.
5. Residential Retro-fit Assistance Fund (RRAF) to be reduced to \$500,000 per year, as proposed in Heritage Gas Rebuttal Evidence.

2.0 GAS DISTRIBUTION ACT

[11] The Application is made under s. 22 of the Act:

Approval and fixing of rates, tolls and charges

22 (1) The Board may, on its own initiative or on the application of a person having an interest, by order in writing, approve or fix just and reasonable rates, tolls or charges for the delivery of gas by a gas delivery system, including related services.

(2) Before approving or fixing rates, tolls or charges pursuant to subsection (1) and subject to the authority of the Board pursuant to subsections 21(1A), (1B), (1C) and (1D), the Board shall invite public comment on the application and, where in the opinion of the Board it is desirable to do so, hold a public hearing.

(3) In approving or fixing rates, tolls or charges, the Board shall give due regard to the following criteria and may give appropriate weight to each of them relative to the others:

- (a) the related practical attributes of simplicity, understandability, public acceptability and feasibility of application;
- (b) freedom from controversies as to proper interpretation;
- (c) effectiveness in yielding total revenue requirements under the just and reasonable return standard;
- (d) revenue stability from year to year;
- (e) stability of the rates, tolls or charges themselves, with a minimum of unexpected changes seriously adverse to existing customers;
- (f) competition;
- (g) fairness of the specific rates, tolls or charges in the apportionment of total costs of service among the different consumers;
- (h) avoidance of undue discrimination in rate relationships;
- (i) efficiency of the rates, tolls or charges in discouraging wasteful use of service while promoting all justified types and amounts of use; and
- (j) such other matters as the Board deems appropriate.

(4) Notwithstanding subsection (3), the Board may, by order in writing, approve or fix just and reasonable rates, tolls or charges that

- (a) are intended to result in cost savings or other benefits to be allocated between the owner of the gas delivery system and its customers; and
- (b) are otherwise in the public interest.

(5) The Board may specify terms and conditions that apply to an order made pursuant to subsection (1) or (4).

3.0 ISSUES

[12] The Board considers that the issues which must be addressed in this Decision are as follows:

- (i) Should the Board approve a reduction in Rate Class 1 commercial customers at, or above, 500 GJs/year Base Energy Charge with pricing flexibility approved as described in Heritage Gas' Rebuttal Evidence?
- (ii) Should the Board approve a depreciation deferral as described in Heritage Gas' Rebuttal Evidence with the carrying cost to be 4%?
- (iii) Should the Board approve the OM&A deferral as described in Heritage Gas' Rebuttal Evidence with the carrying cost of 4%?
- (iv) Should the Board approve that the Base Energy Cost for Rate Class 1 Residential and Small Commercial customers (<500 GJ/year) be reduced by \$0.50 per GJ for bills issued between November 1, 2016, and April 30, 2017, and from November 1, 2017, to April 30, 2018?
- (v) Should the Residential Retro-Fit Assistance Fund be reduced to \$500,000 per year, as described in Heritage Gas' Rebuttal Evidence?
- (vi) Should Rate Class 1 be divided into two rate classes with 500 GJ/year being the threshold?
- (vii) Should the Board impose a sanction on Heritage Gas as recommended by the CPA?
- (viii) Should the CPA be awarded costs?

4.0 POSITION OF THE PARTIES

[13] In its Application, Heritage described the reasons for its request for relief:

4.1 LONG-TERM SUSTAINABILITY AND GROWTH OF THE NATURAL GAS SYSTEM

The retention of RC1 commercial customers (at or above 500 GJs/year) is essential for the long-term sustainability of Heritage Gas' business. These RC1 commercial customers utilize a high percentage of throughput on the system and more importantly, they also represent the highest percentage of delivery revenues for Heritage Gas. To maintain reasonable costs for its ratepayers now and in the future, retaining these RC1 commercial customers is necessary to ensure the viability of the franchise and so that Heritage Gas' natural gas system is well-positioned for growth in the future. All existing ratepayers will

benefit by retaining these customers since the existing costs of operating and maintaining the system will be shared by more customers on the system.

[Exhibit H-1, pp. 8-9]

[14] Heritage argued that a sustainable natural gas system is beneficial for all Nova Scotians in that it provides potential customers with an attractive option, noting it is the most widely used source for residential heating in Canada. Heritage also noted its environmental attributes when compared to furnace oil, arguing that the retention of potential and future RC1 customers will inherently assist the Province in meeting its GHG emission targets.

[15] CPA made extensive submissions with respect to several of the issues, which will be discussed in the Analysis and Findings section, as the issues are identified.

[16] Killam supported the Application, noting:

...Although the financial burden of the deferral is still being partly shouldered by customers it reflects an equitable reduction in the carry cost of Operating, Maintenance & Administrative ("OM&A") expenses.

[Killam Closing Submission, p.1]

[17] The Province supported the Consensus Proposal, stating:

While it is not a signatory to the consensus proposal, the Department of Energy supports the process undertaken by Heritage Gas and the Consumer Advocate to reach an agreement on this matter. Further, the Department supports the Consensus Proposal to the degree that it balances the needs of Heritage Gas for flexibility within Rate Class 1, while limiting the future impact on customers through the reduced carrying costs on the incremental deferrals for depreciation and OMA expenses related to this application.

[Province Closing Submission, p. 2]

5.0 ANALYSIS AND FINDINGS

- (i) **Should the Board approve a reduction in Rate Class 1 commercial customers at, or above, 500 GJ/year Base Energy Charge with pricing flexibility approved as described in Heritage Gas' Rebuttal Evidence?**

[18] The main element of the Application by Heritage is the request for a reduction in the existing Base Energy Charge for RC1 commercial customers whose annual consumption is at, or above, 500 GJs/year.

[19] Article 1 of the Consensus Proposal executed by Heritage and the CA provides for agreement upon:

1. Reduction in Rate Class 1 commercial customers at or above 500 GJs/year Base Energy Charge ("BEC") with pricing flexibility approved as described in Heritage Gas Rebuttal Evidence.

[Exhibit H-19]

[20] Moreover, Heritage has requested that it be given the flexibility, during the course of the Customer Retention Program, to adjust, from time to time, the BEC for RC1 commercial customers (at or above 500 GJs/year) to a level no greater than the current Board-approved rate (prior to this Application) of \$8.685/GJ for such customers, or to no lower than \$3.10/GJ.

[21] In terms of the notification to customers and the Board, Heritage proposed:

... Heritage Gas proposes to file any such rate change with the Board and notify the RC1 commercial customers (at or above 500 GJs/year) two weeks in advance of the proposed effective date of the change. Heritage Gas' notification filing with the Board will include its rationale for the proposed change together with relevant supporting information. Heritage Gas proposes that the Board will approve the change unless there are exceptional circumstances, and will notify Heritage Gas of its decision at least one week prior to the proposed effective date of implementation.

[Exhibit H-1, p. 13]

[22] In its Rebuttal Evidence, it accepted two recommendations of the CA's expert, Scott Rubin: that it would provide 30 days' notice prior to a change in BEC pricing, and that it would not increase the BEC during the months of December to February in any year.

[23] Killam supports the Consensus Proposal to reduce the Base Energy Charge for RC1 commercial customers.

[24] In its closing submissions, the CPA, while not expressly opposing the reduction, submitted that any reduction in the BEC should be subject to certain “availability criteria”, as follows:

- (a) the reduced BEC is only available to existing RC1 commercial customers using 500-4,999 GJs/year;
- (b) the customer must provide notice to HGL that it will request deactivation due to an alternative energy source;
- (c) the customer must submit a notarized affidavit that attests to the fact that but for the reduced BEC, the customer will deactivate from HGL's Gas Distribution System; and
- (d) the customer must submit information that clearly demonstrates the customer's technical and physical ability to convert to an alternative energy source. [Emphasis added]

[CPA Closing Submission, p. 10]

[25] In support of its submission, counsel for the CPA cited the Board's prior Decision in *Re Nova Scotia Power Incorporated*, 2000 NSUARB 72, respecting an application for the approval of a load retention rate.

[26] In its Rebuttal Evidence, Heritage reiterated its submission that the reduction in the BEC is necessary:

As discussed above, Heritage Gas submits that the competitive threat of alternative energy providers is an unprecedented issue and Heritage Gas has requested the rate adjustment and flexibility for the period between 2016-2020 to be able to effectively respond to this issue consistent with appropriate regulatory practice.

The overriding objective of the Customer Retention Program is to preserve the overall well-being of the utility for the benefit of all its customers, both residential and commercial, by retaining larger RC1 customers on the system. These customers contribute significantly to the recovery of Heritage Gas' costs of service. All existing customers will benefit from the retention of RC1 commercial customers who utilize more than 500 GJs/year since the costs of operating and maintaining the system will be shared by more customers on the system.

[Exhibit H-14, p. 16]

[27] With respect to the CPA's submission on the adoption of “availability criteria”, Heritage stated:

However, Heritage Gas never structured its present Application on the basis of customer specific availability criteria, nor on the basis of any other specific load retention tariff. The circumstances facing Heritage Gas are quite different than those in relation to various load retention tariffs which in general provide the opportunity for larger customers to make a specific case for a lower rate based on either economic distress of their business or their business moving to another jurisdiction or alternate supply option. The situation Heritage

Gas faces differs in that there is intensive competition from the propane industry (the very parties that the CPA represents) to the extent that Heritage Gas has already uncontrovertedly demonstrated that significant amounts of customers are leaving its system.

As well, unlike most jurisdictions where the incumbent utility is operating a mature business, Heritage Gas, as noted in its Application, "is still in the developmental stages and must continue to rely on Board-approved proposals to adapt to the current market forces and enable the company to maintain its customer base".

Imposing a customer-specific test would simply place an enormous obstacle on Heritage Gas' proposed program, in that many customers may simply decide to switch to propane or oil rather than go through the process of a detailed review in order to avail themselves of a lower BEC from Heritage Gas. ...

[Heritage Closing Argument, pp. 12-13]

Findings

[28] Based on the evidence presented in the hearing on the merits, the Board considers that its interim approval of the Application to reduce the BEC should be approved for the duration of the requested Customer Retention Program. In its view, granting the requested relief would be in the public interest.

[29] Under s. 22(3)(f) of the *Act*, the Board is also required to give due regard to competition when approving or fixing rates, tolls or changes. A similar provision is not found in the *Public Utilities Act* under which Nova Scotia Power Incorporated is regulated.

[30] The Board is satisfied from the evidence that, on the balance of probabilities, competitive pressures from alternative energy sources are likely to impact the retention of customers by Heritage, as well as the attraction of new customers to its system. As the Board noted in its interim approval, the departure of customers from the system could potentially have serious negative rate impacts on the remaining customers of the Utility, and indeed, perhaps even on the viability of the Utility itself.

[31] There is also a public interest in maintaining a viable alternative energy option for present and future customers of the Utility and promoting the demonstrable positive impact the use of natural gas has on greenhouse gas emissions.

[32] The Board approves the requested reduction in the BEC for RC1 commercial customers (at or above 500 GJs/year).

[33] The Board also approves Heritage's request to have the flexibility to adjust the BEC for RC1 commercial customers between \$8.685/GJ and \$3.10/GJ, in accordance with the notification terms outlined in the Application, and modified in its Rebuttal Evidence. In the latter, Heritage modified two elements of its Application. It agreed that it would provide the Board, the CA and customers with 30 days' notice prior to a change in BEC pricing. Also, it agreed that it would not increase the BEC during the months of December to February in any year.

[34] On the issue of "availability criteria", the Board does not accept the CPA's submission that such qualifications are required to the Customer Retention Program. The Board notes that the CA has not requested the adoption of "availability criteria". Further, despite the CPA's assertion to the contrary, such terms would be administratively burdensome.

[35] Further, the Board accepts Heritage's submission that the context in this matter is different than the circumstances present in a proceeding involving a load retention rate. In the latter, the withdrawal of one or a few large customers from the system is being considered. In such an instance, a thorough review of each customer's circumstances is warranted, given the significant impact the departure of even one customer may have on the Utility and its customers. In the present instance, the Board

is satisfied that the burden on Heritage has been discharged once the Utility has shown a general set of facts which would lead to circumstances in which it is reasonable to conclude that the departure of numerous smaller customers would be likely, or that there would be a potential impact on the attraction of new customers. As noted above, Heritage has demonstrated that likelihood in this instance.

(ii) Should the Board approve a depreciation deferral as described in Heritage Gas' Rebuttal Evidence with the carrying cost to be 4%?

[36] Heritage's request was to "return to full suspension of depreciation of its plant in-service while the reduced BEC is in place." Recognizing Heritage's greenfield status as a new utility, the Board had permitted suspension of depreciation until 2014, when Heritage was ordered to begin to phase in depreciation expense at 25% increments on an annual basis.

[37] Heritage noted that suspension of depreciation would reduce the cost of service and assist in maintaining the Revenue Deficiency Account ("RDA") below the \$50 million cap during the discounted rate period.

[38] Heritage originally proposed that it would record the suspended depreciation as a deferred regulatory asset to be recovered from rates over the useful life of the plant once the suspension is lifted.

[39] At the interim hearing on this matter, the Board deferred approval of this request until the present hearing, but noted the Board's concern about Heritage creating this unusual deferral and then earning its weighted average cost of capital on the deferred amounts. During the IR process, Board staff requested that Heritage comment on various scenarios, including limiting the cost of capital to 4.5%, which Board staff chose as a

reasonable proxy for a long-term cost of debt rate that could be achieved by Heritage's parent company.

[40] In its Rebuttal Evidence, Heritage noted the Board's concerns and proposed that the lower carrying cost of 4.5% on incremental deferred depreciation, and also the OM&A balances, be included as part of the Application.

[41] Heritage noted this amounts to an approximately 50% reduction from the current weighted average cost of capital of 8.94% and a \$5.7 million reduction in cost recovery from the Application, and "removes any potential incremental shareholder profit from the proposed deferrals", which was the concern expressed by the Board.

[42] The Consensus Proposal reduces the interest rate further to 4% rather than 4.5%.

[43] As noted earlier, both the Province and Killam support the Application, as amended by the Consensus Proposal. CPA argued that, while the 4% is a reduction from the original Application, the entire cost of the deferral should be borne by shareholders.

Finding

[44] The Board sees the Heritage proposal, as amended by the Rebuttal Evidence and further amended by the Consensus Proposal, as a reasonable position for the Company to take on this matter. Clearly, in creating the deferral, there is a delay in the shareholder receiving its return of capital invested in the Utility. At the same time, the Board was concerned that the shareholder not be incented to do this by earning its weighted average cost of capital. By reducing the interest earned to 4%, which appears to be lower than the cost of debt of the parent company, and certainly lower than the cost

of debt of Heritage on a stand-alone basis, the shareholder is not unreasonably benefiting from this proposal. Therefore, the Board approves the depreciation deferral, as amended, coincident with the change in the BEC that was effective on March 22, 2016, by virtue of the Interim Order.

(iii) Should the Board approve the OM&A deferral as described in Heritage Gas' Rebuttal Evidence with the carrying cost of 4%?

[45] As noted earlier, Heritage also requested that it be allowed to capitalize 50% of its OM&A expenses while the reduced BEC is in place. Heritage, in its Application, described the action it is taking to reduce its annualized OM&A expenses to approximately \$11 million. In order to achieve these reductions, Heritage will incur implementation costs, bringing the 2016 OM&A expenses to approximately \$11.7 million. Heritage advised that using its current capitalization policy, the revenue requirement, and therefore the RDA, would increase due to the significant reduction in expansion activity. Accordingly, it requested Board approval to capitalize 50% of its gross OM&A while the reduced BEC is in place. Heritage concluded:

The increased capitalization allowance will reduce the net expenses in the revenue requirement, allowing Heritage Gas to retain adequate resources to maintain a safe and reliable distribution system while operating within the RDA cap during this period of discounted rates.

[Exhibit H-1, p. 15]

[46] Like depreciation, the OM&A deferral will have a carrying cost of 4%, so the analysis, on interest, in the section above, applies here as well.

Finding

[47] Similar to the reasoning for the depreciation deferral, the Board approves the OM&A deferral requested by Heritage while the BEC is in effect.

- (iv) **Should the Board approve that the Base Energy Cost for Rate Class 1 Residential and Small Commercial customers (<500 GJ/year) be reduced by \$0.50 per GJ for bills issued between November 1, 2016, and April 30, 2017, and from November 1, 2017, to April 30, 2018?**

[48] This proposal was not part of the original Application, but appeared for the first time in the Consensus Proposal. It is obviously a negotiated term of an agreement between the CA and Heritage that benefits the customers represented by the CA.

[49] Heritage noted that the proposed \$0.50 per GJ reduction for RC1 customers using less than 500 GJs per year is expected to create a revenue deficiency or shortfall of approximately \$466,000 by 2020. However, Heritage argued the reduction of return on the incremental deferred depreciation and OM&A from 4.5% to 4% results in approximately \$500,000 of lower financing costs, which is a direct decrease in amounts payable to the shareholder, and that the shareholder provides 100% of the debt of Heritage. Heritage witness, Zeda Redden, discussed the impact of this:

MS. REDDEN: You'll note that in the rebuttal evidence that we submitted that we had proposed a 4.5 percent return on the deferred depreciation and balances. As part of the settlement, we agreed to reduce that to 4 percent.

Lowering the return from 4.5 to 4 percent more than offsets the change to the RDA that arises from giving the 50 cent per GJ reduction in rates to the lower Rate Class 1s so, in effect, the shareholder is funding the reduction in that rate to the Rate Class 1s by the reduction of the return in ---

THE CHAIR: Can you give us the comparison numbers; in other words, for the two heating seasons, that they get the 50-cent reduction?

MS. REDDEN: The cost is about 500,000.

THE CHAIR: Per season, or in total?

MS. REDDEN: In total.

THE CHAIR: And the difference between -- it's in your evidence, but just remind me, the difference between 4.5 and 4 is?

MS. REDDEN: It's between 500,000 and 600,000.

THE CHAIR: Thank you.

[Transcript, pp. 62-63]

[50] The CA's expert, Scott Rubin, spoke in support of the deferral:

... In addition, there is a modest benefit to existing customers with the 50 cent per gigajoule reduction in the BEC for the next two heating season -- seasons, excuse me. I estimate the value of that to be in the -- around 225 to \$250,000 per year. If that reduction were in place for the entire year, it would be about \$260,000. The heating season accounts for probably between 80 and 90 percent of annual gas usage. So I'm estimating about 225 to \$250,000 annually for two years.

That's a modest benefit for residential customers. I doubt that would be enough to give a customer an incentive to not switch to propane or -- but it is a recognition that residential customers also are affected by what's been happening in the energy markets and, you know, the company has some longer term plans in place to try to bring down the cost of gas. There was a discussion earlier about the storage plans. There's also the reversal of flow on the Maritimes & Northeast Pipeline which would enable some lower cost shale gas to move from the United States into Atlantic Canada.

So there's some longer-term prospects to bring down costs for residential customers and that 50 cent reduction for two heating seasons is a way of, you know, trying to bring some relief to the current winter pricing. And, frankly, it's also a recognition that all customers will be paying in the future as a result of the very large deferrals being built up.

[Transcript, pp. 127-128]

[51] The CPA opposed this reduction to residential and small commercial customers, arguing there is no evidentiary basis to reduce the BEC. The CPA went on to state:

As to the RC1 Residential and Small Commercial customers, there is no evidentiary basis to reduce the BEC. It has not been proposed as a load retention rate but rather to offer "support" to those customers. HGL is adamant it is able to and does effectively compete in the residential markets with propane suppliers based on the current rates being offered. In fact, out of its 3,300 residential customers, only 19 customers have converted since January 1, 2015 (11 of those were properties owned by one person).

Effectively, the seasonal discount proposed was the cost of the deal with the CA - which, perhaps not coincidentally is silent regarding the CA's recommended sanction, discussed further below.

Part of the *quid pro quo* with the CA and the basis for which HGL argues the residential discount should be approved is that it has agreed to a reduced carrying cost on the deferred depreciation and OMA from 4.5% to 4% so the "net effect" or the "end result" on a financial basis is described as a shareholder cost.

With respect, there is already a substantial revenue/cost gap for the residential and small commercial customers. Mr. Rubin calculated the R/C ratios of the residential and small RC1 commercial customers at 29% and 55% respectively at the existing RC1 BEC; HGL believes the average costs to serve these customers are somewhere between 2.7 and 3.5 times the revenue generated at current rates.

...

Reducing the SEC to small RC1 customers runs counter to cost-of-service principles, and is not warranted under any rate retention rationale.

The CPA suggests that if HGL wishes to make this a shareholder cost in fact and not just "in effect," such that the revenue shortfall is a shareholder cost and not added to the Revenue Deficiency Account ("RDA"), it may do so (and this is reflected in its accounts as such). However, CPA respectfully submits that there is no evidentiary basis to reduce the BEC to these customers and this aspect of the "Consensus Proposal" should not be approved.

[CPA Closing Submission, pp. 5-6]

Findings

[52] Heritage presents this as an arrangement whereby it agreed to lower the return on the deferrals by one half percent, and that more than offsets the cost that arises from giving the \$0.50 per GJ reduction in rates to the small RC1 customers. So, "...in effect the shareholder is funding the reduction." In other words, the rate class reduction is funded by the reduction in return that the shareholder is foregoing.

[53] Mr. Rubin originally argued for a larger reduction in the rates to the small customers, noting that competitive pressures and costs affect the small customers as well. However, there is a lack of evidence to show that the small customers were leaving the Heritage system although, arguably, they may do so.

[54] Frankly, the Board is troubled by this portion of the Consensus Proposal as it appears as being put forward only as "part of the deal". The Board has indicated in the past that it understands the components of a settlement agreement are inter-related and subject to compromise, and the Board must take care not to alter one component, as it may unbalance the overall result.

[55] For purposes of this Application, the Board will accept Heritage's argument that, in order to finance this reduction, the Company compromised the amount of interest it would earn on the deferrals, thereby making this "in effect" a shareholder cost. The

Board is prepared to approve this reduction so long as the cost of the reduction is less than the amount saved by lowering the rate of return. Heritage is to monitor this and report to the Board every six months during the period of the reduction, as part of its financial reporting, and if circumstances arise such that the lowering of the return is not financing the lowering of the rate, then the Board will intervene.

(v) Should the Residential Retro-Fit Assistance Fund be reduced to \$500,000 per year, as described in Heritage Gas' Rebuttal Evidence?

[56] The Residential Retro-Fit Assistance Fund ("RRAF") cap was \$5 million, as approved by the Board in proceeding 2016 NSUARB 15 (M07146).

[57] Heritage, in its Rebuttal Evidence, in responding to comments made by Mr. Rubin in his evidence, agreed that faced with the current circumstance, it is prudent for the Company to limit the utilization of the RRAF while the Customer Retention Program is in place. Therefore, Heritage, as noted in the Consensus Proposal, proposed to limit the utilization of the RRAF to \$500,000 annually, while the Customer Retention Program is in place. This, Heritage argued, still leaves the Program in place to provide flexibility to address highly strategic projects which might materialize.

Finding

[58] The Board approves this reduction.

(vi) Should Rate Class 1 be divided into two rate classes with 500 GJ/year being the threshold?

[59] Killam recommended, in evidence and in its final argument, that the Board and Heritage should continue efforts to implement a new rate class for larger RC1 customers. This was also raised by the Board in the hearing, and Heritage was asked to

provide an undertaking with respect to this issue. In Undertaking U-4, Heritage cited an extract from the Chymko Report on Cost of Service, filed as part of Heritage Gas GTA 11. At that time, Chymko did not recommend changes to the class boundaries, noting that, while the results do demonstrate cross-subsidization, it was not necessarily inappropriate given the seven year old gas distribution utility. Chymko noted that, should potential customers convert to natural gas, the density of the distribution network will improve and the average cost to customer will decline. Heritage went on to say:

While no cost of service study was conducted as part of the Customer Retention Program Application, Heritage Gas notes that neither the residential nor the small commercial customer (i.e. less than 500 GJs/year) sub-groups within Rate Class 1 appear to cover their cost of service. A full cost of service study is required to specifically quantify the gap between revenue and cost to serve them, but it appears that there is a sizable gap. In fact, based on simplified calculations, Heritage Gas believes the average cost to serve for these customers is somewhere between 2.7 and 3.5 times the revenue generated at current rates. In other words, rates would have to go up by at least 170% should these customers be segregated into their own rate class today. In Heritage Gas' view, a rate increase of this magnitude would definitely constitute rate shock and would drive most, or all, of these small customers (both current and future) away from the natural gas distribution system, resulting in a substantial loss of revenue but not a substantial decrease in the cost of service. The majority of these costs would simply shift from the small customers to larger customers resulting in rate increases for them.

[Exhibit H-20, Response to U-4, p. 2]

Finding

[60] There was no cost of service evidence filed in this proceeding. Accordingly, it would be inappropriate for the Board to create a new class at this point. However, the Board directs Heritage to re-examine this, including appropriate cost of service evidence, as part of the next general rate application.

(vii) Should the Board impose a sanction on Heritage Gas as recommended by the CPA?

[61] In its written submissions following the hearing, the CPA requested that the Board sanction Heritage as a result of its alleged non-disclosure of information in the

recent hearing relating to the Residential Retro-fit Assistance Fund. In its Decision dated February 22, 2016, and reported at 2016 NSUARB 15, the Board approved an increase in the RRAF from \$1 million per year to \$5 million per year.

[62] The circumstances which laid the foundation for the CPA's submission on this point were raised in the pre-filed evidence of Scott Rubin, the CA's expert. Mr. Rubin alleged that Heritage presented favourable projections to the Board in the RRAF application, but failed to advise the Board when it became aware that those forecasts had changed significantly to the negative. In his report, he stated:

At no time in that case -- either in its initial filing on October 29, its supplemental filing on December 9, 2015 (just days two weeks [sic] before the Company presented its "Action Plan" to AltaGas), or in its IR responses on January 11 -- did the Company indicate that it was in serious peril because of competitive fuel markets. At no time during the pendency of that case did the Company come to the Board and parties to correct the faulty impression that this was a growing company expecting to add hundreds of new commercial customers each year. At no time did the Company inform the Board and the parties that the RDA would be increasing significantly because it was losing dozens of customers. And certainly at no time did the Company inform the Board and the parties that the Company was facing serious cash-flow problems that would result in laying off employees, reducing OMA significantly, and canceling all but the most essential capital projects. That case was not decided until February 22, 2016 -- after Heritage Gas's Board of Directors approved the emergency measures sought in this case and after AltaGas's executive committee approved that plan -- yet Heritage Gas never informed the Board or the parties of the true financial and competitive position of the Company.

[Exhibit H-10, p. 23]

[63] Mr. Rubin had filed evidence on behalf of the CA in the RRAF matter. In the present proceeding, Mr. Rubin indicated that he had "relied on the truthfulness and accuracy of the Company's [RRAF] application, IR responses, and other submissions in formulating my conclusions and recommendations in that case" [Exhibit H-10, p. 24].

[64] In her written submissions, counsel for the CPA asked that the Board impose a sanction on Heritage in the range of \$100,000 to \$250,000. She refers to the Board's Decision in *Re Nova Scotia Power Incorporated*, 2012 NSUARB 227, as support for the Board imposing a sanction upon Heritage.

[65] While it was Mr. Rubin, the CA's expert, who raised this issue, the CA did not take a position on the CPA's request for a sanction. Indeed, Ms. Rubin intimated there was a link between the negotiation of the Consensus Proposal and the CA's silence on the point:

Effectively, the seasonal discount proposed was the cost of the deal with the CA - which, perhaps not coincidentally is silent regarding the CA's recommended sanction, ...

[CPA Closing Submission, p. 5]

[66] Heritage opposed the imposition of a sanction:

The CPA is not even arguing with respect to Heritage Gas' conduct in this Hearing, but rather is making an argument that Heritage Gas should be sanctioned because the utility's current plans for utilization of the Residential Retro-fit Assistance Fund ("RRAF") are within the previously approved amount and therefore, the CPA argues, the RRAF application, not this Hearing, was unnecessary. The timelines and explanations for when information was available and provided to the Board and intervenors are well set out in the record of this proceeding, and do not support the CPA's contention.

Further, the CPA appears to rely on section 31 of the *Gas Distribution Act* ("GDA") for the proposition that the Board has the authority to sanction Heritage Gas in the present circumstances. However, section 31 of the GDA deals with awards of costs not sanctions. As noted below in regard to the CPA's claim for legal costs, section 36 of the *Gas Distribution Regulations* specifically provides that pursuant to section 31 of the GDA costs of and incidental to any proceeding before the Board are in its discretion and may be fixed at a sum certain or may be taxed. As is made clear from the wording of section 31 of the GDA and section 36 of the *Gas Distribution Regulations*, these provisions deal with claims for costs as between parties "at the conclusion of a hearing", not sanctions.

[Heritage Reply Argument, pp. 2-3]

[67] In its Rebuttal Evidence, Heritage indicated it would limit the utilization of the RRAF to \$500,000 annually while the Customer Retention Program is in place, to provide a limited degree of flexibility to address highly strategic projects which may materialize.

Finding

[68] The Board is responsible for the general supervision of Heritage under the *Gas Distribution Act* and the *Regulations*. In addition to s. 22 quoted earlier in this

Decision, the Board's authority under the *Act* includes:

Approved tariff

21 (1) The holder of a franchise shall not impose, observe or follow rates, tolls or charges except those that are specified in a tariff that has been filed with the Board and approved by an order of the Board.

(1A) When the holder of a franchise has submitted, for the approval of the Board, a schedule of rates, tolls and charges, or a proposed change in any existing schedule of rates, tolls and charges, that, in the opinion of the Board,

(a) constitutes a reduction in the existing schedule of rates, tolls and charges at the time being paid by the majority of the customers of such franchise affected by such change in the class of service to which such proposed change applies; or

(b) applies only in respect of a service for which no rates, tolls or charges have been previously approved,

the Board may, at any time before finally approving or disapproving the schedule or change, grant an interim approval with or without conditions.

(1B) The schedule of rates, tolls and charges of the franchise, as approved by the Board pursuant to subsection (1A), shall be filed with the Board and are the only lawful rates, tolls and charges of the franchise until altered or modified in accordance with Section 22.

(1C) Notwithstanding anything contained in this Act, the interim approval granted pursuant to subsection (1A) may be given *ex parte* and without public hearing or notice.

(1D) Where the holder of a franchise has been granted an interim approval pursuant to subsection (1A), the holder of the franchise shall make an application to the Board within one hundred and eighty days for final approval.

(2) Where the holder of a franchise is the only customer of that franchise, the Board may exempt the holder of the franchise from the requirements of subsection (1).

...

Costs

31 (1) At the conclusion of a hearing, the Board may award such costs as the Board deems appropriate.

...

Investigations

34 The Board may, on its own initiative or at the request of the Governor in Council, investigate any matter concerning a gas delivery system and may make all necessary examinations and inquiries and keep itself informed as to the compliance of the holder of a franchise with the provisions of law and has the right to obtain from the holder of a franchise all information necessary to enable the Board to fulfil its duties.

...

False statement

39 No person shall knowingly make a false statement in any record required to be kept or any document required to be submitted pursuant to this Act or the regulations.

[69] The Board is mindful of Mr. Rubin's concerns regarding the failure of Heritage to disclose material information to the Board, which could have impacted its RRAF application. It finds Heritage's conduct, in failing to disclose the material information, to lack the necessary diligence the Board would have expected in the circumstances.

[70] The Board relied on Mr. Rubin's evidence in the RRAF matter in approving the program. As a result, it shares his concerns. However, the Consumer Advocate, who sponsored Mr. Rubin's evidence, does not support the sanction request.

[71] Given Heritage's knowledge of the financial circumstances it was in at the time it pursued the RRAF with the Board, or at least at the time of the Board's consideration of the matter, it is reasonable to conclude that the Board, if it had been made aware of those material facts, may not have approved the program, or it may have considered a reduced scope for the program. The Board observes here that it is not suggesting that Heritage intentionally tried to mislead the Board, simply that it should have shown greater diligence in advising the Board of a material change in the facts supporting that application.

[72] The Board notes that the implementation of the RRAF itself was identified by Heritage during this Application as an item where Heritage could reduce or contain costs. As noted above, Heritage has undertaken to limit the utilization of the RRAF to \$500,000 annually while the Customer Retention Program is in place.

[73] As the Board noted in its 2012 *NSPI* Decision, any sanction imposed should relate directly to actions of Heritage, including specific instances where it has showed imprudence or ignored direction from the Board. In *NSPI*, the Board stated:

...Moreover, NSPI's course of action had the effect of wasting scarce resources, in terms of time, money and human resources, for all parties, notably those of the Intervenor who participated in this proceeding, including experienced legal counsel and, likely in some cases, their expert consultants. This conduct resulted in increased costs for all Intervenor, including those representing most customer classes served by the Utility.

[NSPI Decision, 2012 NSUARB 227, para. 415]

[74] The Board considers that the circumstances in the present instance are distinguishable from those in *NSPI*. First, as noted above, the party who retained Mr. Rubin and filed his evidence does not support the sanction request made by the CPA. The Consumer Advocate signed the Consensus Proposal and offered no submissions on the sanction issue. Second, the RRAF matter is an entirely different proceeding than the present matter.

[75] Accordingly, the Board finds that the imposition of a sanction is not warranted. However, if similar circumstances were to arise in the future, the Board would seriously consider imposing an award of costs against Heritage to account for the waste of time, money, and effort by counsel and the Board in dealing with such an issue.

(viii) Should the CPA be awarded costs?

[76] The CPA has asked for costs with respect to its participation in the hearing. The CPA did not retain a consultant or expert in this matter, but seeks costs for its legal counsel. In her written submissions following the hearing, Ms. Rubin stated:

CPA is a non-profit organization. Its members have a substantial interest in the outcome of this proceeding and will be affected thereby. It is respectfully submitted that CPA participated responsibly in this proceeding, including in the Interim Application, through its IRs, cross-examination and submissions, and in doing so, it contributed to a better understanding of the issues by the Board, including issues it advanced which benefit the public interest. CPA alone fleshed out considerations of evidentiary proof of necessity for the tariff, availability criteria and free-ridership.

[CPA Closing Submission, p. 9]

[77] Ms. Rubin described her client's circumstances as analogous to those of the Urban Development Institute ("UDI") in the matter of an application by the Halifax

Regional Water Commission for a regional development charge: *Urban Development Institute of Nova Scotia v. Halifax Regional Water Commission*, 2014 NSUARB 128. UDI was a non-profit organization formed by members of the development community in this province to advocate on issues impacting the industry.

[78] Heritage opposed the request for costs. In his written submissions on behalf of Heritage, Mr. Johnston stated:

The CPA and UDI are not comparable intervenors. While the CPA is incorporated as a not-for-profit industry association, the CPA's Membership List indicates that many of the over 400 companies the CPA represents are Canadian multinational companies in the production, transportation and retailing of propane in Canada. Indeed, the CPA's website describes itself as the "...national voice of the Canadian propane industry, a multi-billion dollar industry...". In contrast, UDI represented only approximately 100 members from the development community in Nova Scotia.

The CPA is also clearly not an organization with limited financial resources, as required by Rule 6(2). UDI's typical annual budget was around \$50,000 and its surplus was less than \$35,000. According to the CPA's 2016 Membership Fee Table, the CPA's membership fee of \$75,494 for a single member who retails 1.2 million cubic metres of propane alone exceeds the annual budget for UDI. The financial means of UDI and the CPA are simply incomparable; the organizations are on entirely different scales.

Unlike UDI, which was run by a volunteer board of directors and a part time manager, the CPA's website lists 12 staff members in its Ottawa and Calgary Offices, including an Executive Director, ... The fact that the CPA has staffed positions to deal specifically with regulatory affairs demonstrates that the CPA has ample financial means and the ability to budget for and staff participation in regulatory proceedings such as this matter.

[Emphasis in original]

[Heritage Reply Argument, pp. 9-10]

[79] Further, Heritage submitted that the CPA was not a "public interest" intervenor, in that it advanced the private interests of Heritage's primary competitors, none of which are customers of Heritage.

Findings

[80] Legal counsel for the CPA refers to s. 31 of the *Act* and s. 36 of the *Gas Distribution Regulations (Nova Scotia)* in support of its request for costs:

36 (1) Pursuant to Section 31 of the Act, party and party costs and solicitor-client costs of and incidental to any proceeding before the Board are in its discretion and may be fixed at a sum certain or may be taxed.

(2) The Board may order by whom and to whom any costs are to be paid and by whom they are to be taxed and allowed.

(3) The Board may prescribe a scale under which such costs shall be taxed.

(4) In awarding costs, the Board is not limited to the considerations that govern awards of costs in any court.

[81] Further, as noted by Heritage, s. 6 of the Board's *Costs Rules* also provide:

- 6 (2) The Board may consider awarding costs against a utility to non-profit, public interest intervenors with limited financial resources who
- (a) have a substantial interest in the proceeding;
 - (b) will be affected by the proceeding;
 - (c) participate in the hearing in a responsible way; and
 - (d) contribute to a better understanding of the issues by the Board.

[82] While the CPA argued that the Board's jurisdiction to award costs is broader under s. 36 of the *Gas Distribution Regulations (Nova Scotia)* than under the Board's *Costs Rules*, the Board considers that CPA's request for costs should be denied under either provision.

[83] Most of the arguments advanced by the CPA at the hearing on the main issues were not accepted by the Board. Specifically, the Board did not accept CPA's submission that "availability criteria" should apply to Heritage's customers requesting a reduction in the BEC; and the Board allowed Heritage's request to extend the BEC reduction to residential and small commercial RC1 customers.

[84] Moreover, the Board concludes that the interests advanced by the CPA were, in effect, for the benefit of the private interests of its own members, who are competitors of Heritage, rather than the public interest.

[85] Taking all of the above into account, the Board denies CPA's request for costs.

6.0 COMPLIANCE FILING

[86] Heritage is directed to file a Compliance Filing as soon as conveniently possible.

[87] The Formal Intervenors are to provide comments, if any, no later than one week later, with a reply from Heritage, if required, one week later.

7.0 SUMMARY

[88] The Board approves Heritage's Application to have the flexibility to adjust, from time to time, the Base Energy Charge for RC1 commercial customers whose annual consumption is at, or above, 500 GJs/year, to a level no greater than the current Board-approved rate (prior to this Application) of \$8.685/GJ for such customers, or to lower the BEC to no lower than \$3.10/GJ. Heritage must provide the Board, the Consumer Advocate and customers with 30 days' notice prior to a change in BEC pricing. Also, it will not increase the BEC during the months of December to February in any year.

[89] Further, the Board approves the suspension of depreciation of Heritage's plant-in-service while the reduced BEC is in place, and grants its request to capitalize 50% of its Operating, Maintenance and Administrative ("OM&A") expenses while the reduced BEC is in place. For each of these two deferrals, the carrying cost shall be limited to 4%.

[90] The above Customer Retention Program shall be in effect until December 31, 2020, unless otherwise ordered by the Board.

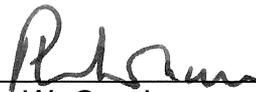
[91] The Board also approves the request by Heritage, as contained in the Consensus Proposal with the Consumer Advocate, that the Base Energy Cost for Rate

Class 1 Residential and Small Commercial customers (<500 GJs/year) be reduced by \$0.50 per GJ for bills issued between November 1, 2016, and April 30, 2017, and from November 1, 2017, to April 30, 2018.

[92] Finally, the Board approves the reduction of the Residential Retro-Fit Assistance Fund from \$5 million per year to \$500,000 per year.

[93] An Order will issue upon receipt of the Compliance Filing and submissions.

DATED at Halifax, Nova Scotia, this 8th day of September, 2016.



Peter W. Gurnham



Roland A. Deveau