**Written Argument of Direct Energy Marketing Limited**

**Re: "The Jurisdictional Question" posed by the Ontario Energy Board in EB-2009-0172, Procedural Orders No.1 and No.2**

## Background

Enbridge Gas Distribution Inc. (EGD) filed an Application on September 1, 2009 with the Ontario Energy Board (the Board) seeking approval of rates for the distribution, transmission, and storage of natural gas, effective January 1, 2010, including the request for Y-factor treatment of non-descript renewable energy activities. On September 8, 2009 the Minister of Energy and Infrastructure issued an Order in Council allowing EGD and Union Gas Ltd to own and operate renewable energy electricity generation facilities, in a similar manner as electricity distributors. EGD then filed evidence in relation to its Application on October 1, 2009, seeking in part, approval for the capital, maintenance, and operating costs associated with its "Green Energy Initiatives"[1], to be included as a component of total rate base for rate making purposes.

On October 1, 2009 the Board issued Procedural Order No. 1, determining that as a preliminary matter, whether "electricity generation facility projects and their associated costs, assets and revenues, are properly part of the regulated operations of Enbridge"[2]. The Board further clarified their position based on the written argument of EGD in this proceeding filed on November 4, 2009, such that the preliminary matter should examine all of EGD's Green Energy Initiatives. As such, on November 9, 2009 the Board issued Procedural Order No.2, requesting comments on the two jurisdictional questions posed:

1. Are the Green Energy Initiatives described in Enbridge's Application (Ex. B, Tab 2, Sch. 4), their associated costs, assets and revenues properly part of the regulated operations of Enbridge and thus under the Board's ratemaking authority?

2. If not, does the Board have jurisdiction to deal with the Green Energy Initiatives, their associated costs, assets and revenues outside of the ratemaking process?

For the reasons set out in the following submission Direct Energy (DE) believes that , regardless of whether the Board has the jurisdiction to deal with EGD's Green Energy Initiatives, the costs, assets, and revenues of these initiatives are not properly part of the regulated operations of EGD, and should therefore be excluded from rate base.

## Precedent and consistency in policy making

On May 14, 2009 the Green Energy Act (GEA) received Royal Assent, and certain provisions within the GEA allowing electricity distribution companies (LDCs) to own and operate renewable generation facilities were proclaimed into force on September 9, 2009. On September 15, 2009 under EB-2009-0300 the Board issued its Guidelines for the Regulatory and Accounting Treatments for Distributor-Owned Generation Facilities ("the Guidelines").

In Section 2.2 of the Guidelines, entitled "Legislative Limitation on Rate Regulation", the Board found that:

[1] Examples found in Ex. B-2-4 para 1
[2] Procedural Order No.1, pg 4, para 4

> "Section 78(3) of the OEB Act only permits the Board to set rates for the transmission and distribution of electricity and for the retailing of electricity. The statutory framework does not currently give the Board the power to include generation assets in rate base, nor to permit rate recovery for any associated operations and maintenance expenses for distributors."

In a similar manner, the OEB Act describes the rate making authority of the Board for natural gas utilities in Section 36(2) as:

> "The Board may make orders approving or fixing just and reasonable rates for the sale of gas by gas transmitters, gas distributors and storage companies, and for the transmission, distribution and storage of gas. 1998, c. 15, Sched. B, s. 36 (2)."

As can be seen by the similarities between the two above noted sections of the OEB Act, it would stand to reason that the Green Energy Initiatives applied for by EGD in this case, should be treated in a similar manner to the "green" renewable generation assets held by LDC's. Furthermore, section 71 (3) of the OEB Act mandates an electricity distributor to "keep its financial records associated with distributing electricity separate from its financial records associated with other activities". There is no reason as to why similar "green" investments made by gas utilities should be treated any differently.

Throughout their Argument in this case, EGD has advocated for similar treatment of energy issues as a whole; in that the treatment of natural gas issues should be similar to the treatment of electricity issues. EGD has even gone so far as to purport that it is Government Policy to ensure consistent application of policy in energy matters[3]. It would appear though, that EGD is in fact asking for special treatment for the Green Energy Initiatives in its Application, distinctively different from the manner in which the Board has prescribed treatment for similar activities by electricity LDCs.

The Board has already determined that the Government's direction to allow LDC's to own and operate renewable generation facilities as a means to further the Government's green initiatives, does not establish that such green energy projects could be funded by rate payers. In fact, the Board was very specific in determining that such initiatives could <u>not</u> be funded by rate payers. The Guidelines provide two means for LDCs to own and operate generation facilities:

> <u>Section 3.1: Generation Facility Owned by an Affiliate</u>
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> "Affiliates of distributors are currently permitted to own and operate generation facilities; this situation will not be altered by the Green Energy Act. Any new generation facility owned or operated by an affiliate of a distributor would continue to be governed by the current rules, including the requirement for compliance with the Affiliate Relationships Code (ARC) for Electricity Distributor and Transmitters and the requirement to provide notice to the Board under s. 80 of the OEB Act."
>
> <u>Section 3.2: Generation Facility Owned by Distributor and Non-Rate Regulated</u>
>
> "A distributor may also choose to own and operate a generation facility directly as part of its utility business. Under this scenario, ***costs would not be recovered through rates and a regulatory return would not be earned on the investment.*** [Emphasis added] The investment project would be debt and/or equity financed. The distributor may enter into a feed-in tariff (FIT) contract with the Ontario Power Authority (OPA). These contracts are long-term in nature and the energy prices vary depending on the type of generation technology and the capacity of the facility."

[3] Enbridge Submissions on jurisdictional question, pg 12, para (d)

Clearly the Board has already set precedent in this matter. In order for the Board to be consistent in its application of policy between natural gas and electricity as EGD so desires, the Board must find it necessary to exclude any assets from the regulated operations of Enbridge that are not related to the sale, distribution, transmission, and storage of natural gas. As noted at the top of page 11 in EGD's Argument, "Not one of the policy objectives supports the notion that the government's policies are compatible with a compartmentalized approach to electricity and gas matters." Based on this statement, it would seem that EGD should be agreeable to the Board treating "green" natural gas initiatives in the same manner as it does "green" electricity initiatives.

Finally, while the Minister's Directive of September 8, 2009 granted EGD the right to own and operate green energy initiatives in a similar manner to electricity LDCs, it explicitly stated that the "directive is not in any way intended to direct the manner in which the Ontario Energy Board determines, Under the Ontario Energy Board Act, 1998, rates for the sale, transmission, distribution and storage of natural gas by Enbridge Gas Distribution Inc. and Union Gas Limited." DE submits that the Minister has acknowledged that the ratemaking authority of the Board is separate and apart from the Directive.

Regulatory process and definition of "Green Energy Initiatives"

It appears that the matters currently before the Board in this Application have fallen into a regulatory gap between the timing of the Minister's Directive on September 8th of this year, and the filing of EGD's evidence on October 1st. The Board has already prescribed treatment for LDC green initiatives through the Guidelines issued on September 15th of this year, yet there is an absence of similar guidelines and treatment for natural gas utilities. Furthermore the definition of renewable generation and related activities may be beneficial. Enbridge claims on page 4 of its Argument that solar, ground source heat pumps, District Energy systems, heat from waste technologies and geo-thermal systems would not be considered to be "electricity generation facility projects", and therefore leads EGD to (inappropriately) assume that their associated costs, assets and revenues fall under the Board's rate making authority. However, Section 2 (1) of the Electricity Act, 1998, S.O. 1998, c. 15, Sched. A, appears to have a divergent view from EGD. Most, if not all of these items are recognized as renewable energy sources. The definition of a Renewable Energy Source as described in the Act is as follows:

> "renewable energy source" means an energy source that is renewed by natural processes and includes wind, water, biomass, biogas, biofuel, solar energy, geothermal energy, tidal forces and such other energy sources as may be prescribed by the regulations, but only if the energy source satisfies such criteria as may be prescribed by the regulations for that energy source;"

Additionally, district energy systems are not an extension of natural gas distribution systems. EGD's distribution system, whose rates are appropriately reviewed by the Board, are solely for the purpose of selling and distributing natural gas. District energy systems carrying heating, cooling, or hot water are systems unto themselves, not unlike the internal distribution systems within customers' homes. But unlike EGD's natural gas distribution system, district energy is not for the benefit of all ratepayers in EGD's franchise area, but for a select group of individuals and businesses partaking in commercial arrangements.

It is the commercial nature of these activities that must be recognized and determined by the Board to be outside of its rate making authority. As with LDCs, such activities should be conducted either through an Affiliate or without the ability to recover costs and regulated returns on the investment through rate base.

**Balancing Board objectives and the commercial nature of EGD's request**

In its Argument in this case, EGD has inappropriately attempted to link the Board's authority to Government policy in the narrowest of terms. EGD claims that "In carrying out its responsibilities with respect to gas, the Board is to be guided by the objective of promoting energy conservation and energy efficiency in accordance with the policies of the government of Ontario."[4] It would seem that EGD has failed to recognize that, amongst many other obligations, two of the primary objectives of the Board in both Gas and Electricity are to facilitate a viable energy sector and provide consumer protection with respect to rates.

The first two objectives of the Board with respect to electricity in Section 1. (1) of the OEB Act are:

1. To protect the interests of consumers with respect to prices and the adequacy, reliability and quality of electricity service. and;
2. To promote economic efficiency and cost effectiveness in the generation, transmission, distribution, sale and demand management of electricity and to facilitate the maintenance of a financially viable electricity industry.

The market structure and consumer protection objectives of the Board are just as clear for natural gas, as Section 2 of the OEB Act states in part:

> "The Board, in carrying out its responsibilities under this or any other Act in relation to gas, shall be guided by the following objectives:
>
> 1. To facilitate competition in the sale of gas to users.
>
> 2. To protect the interests of consumers with respect to prices and the reliability and quality of gas service."

By requesting its Green Energy Initiatives to be included as a component of total rate base for rate making purposes[5], it would seem that EGD is concerned about the electrification of the Ontario energy market, and its impact on future revenues[6]. If the Board were to grant such a request, it would create a "no risk" scenario for Enbridge shareholders, while imposing an "all risk" scenario for distribution customers. The projects proposed by Enbridge appear to be commercial in nature, as they are not related to the sale, transmission, distribution, or storage of gas. As such, EGD should be subject to the same market conditions, investment opportunities, risks, and payback periods as any other commercial entity.

The commercial nature of EGD's request can be found in Exhibit B-2-4, paragraphs 1 and 16, whereby EGD states:

> " the Company plans to pursue initiatives and **own and operate a variety of assets capable of generating and distributing alternative forms of energy to end-use customers** in Enbridge's franchise areas. Through these initiatives, **Enbridge would design, market, invest in, own and operate assets** that will primarily focus on providing space heating and cooling and domestic hot water for its customers"[7]; and

[4] Enbridge Submissions on jurisdictional question, pg 8, last paragraph
[5] Ex. B-2-4; para 16
[6] Ex-B-2-4; para 10
[7] Ex. B-2-4; para 1

> "Enbridge proposes that **Green Energy Project assets would be included in the regulated utility and would be a component of total rate base for ratemaking purposes**. Operating costs and revenues associated with these projects would be included when calculating the utility revenue requirement and any deficiency/sufficiency for ratemaking purposes. At this time, **Enbridge expects that the amounts to be charged to customers connecting to these projects would be set by contract. As a result, it will not be necessary for the OEB to establish rates for these customers.**"[8]
> [Emphasis added]

EGD has claimed that these projects have high initial capital costs with relatively long pay-back periods, and that in order for the projects to be viable they must be treated in the same manner as other regulated activities[9]. This would indicate that EGD recognizes that it would have a considerable advantage over other suppliers of green energy projects if it were able to recover any initial losses in the start up years of these projects from rate base, while reaping the rewards of revenue sharing in later years. In allowing Enbridge cost recovery, the Board would create an unfair advantage for Enbridge over other suppliers in this space, diminishing the private investment and efficiencies that come with fair and open competition. It would also ultimately result in ongoing higher costs for ratepayers, as the costs for the maintenance, upgrades, and obsolescence of these new technology assets will be borne by the ratepayer, and not the private sector. As mentioned earlier, the Board has already established in the Guidelines that investment projects should be debt/equity financed, and where possible, companies should avail themselves of the lucrative feed-in tariff contracts provided by the Ontario Power Authority.

It is clear from the provisions contained within the OEB Act that the Board has a responsibility to ensure economic efficiency and cost effectiveness while providing price protection to consumers. DE submits that the Board would be unable to uphold these committed objectives, if it were to approve EGD's request to include its "Green Energy Initiatives" inside of regulated activities. DE also agrees with Board staff that the viability of these initiatives is independent of their inclusion in regulated operations.[10]

**Ancillary Services**

On page 16 of EGD's Argument, EGD attempts to support its position for recovery of costs by stating that the Board had previously allowed ancillary businesses such as merchandise sales and protection programs for heating to be included within gas utility operations. It also noted that the Board did not set the price for these services, but included the results in utility operations. EGD fails to mention however that over a decade ago, the Board found that ancillary services such as the rental water heater program should not be part of the regulated operations of EGD, and ordered these services to be unbundled from rate base[11].

The Board look no further than the unbundling of ancillary services from natural gas utilities as to why it should not allow recovery of costs from rate base for the activities proposed by EGD in this proceeding. In Enbridge's case, the assets, products, and services initially funded by rate payers that were separated into a retail division of the company, were eventually sold by Enbridge for hundreds of millions of dollars. It is inappropriate for rate payers to fund assets and ancillary services that are not part of the natural gas distribution system, which will ultimately be owned by the private shareholders of Enbridge. The citizens of Ontario are already faced with a $20 billion deficit, and as such ratepayers in EGD's franchise area should not be subject to what amounts to be an economic development tax in order to support the commercial activities of the company. Any movement by the Board to include ancillary services such as

[8] Ex. B-2-4; para 16
[9] Ex. B-2-4, para 13
[10] Board staff submission on "Jurisdictional Question" EB-2009-0172; pg 12
[11] EBO 179-14/15

those proposed in EGD's Green Energy Initiatives would be considered as a step backwards in the evolution of this market, resulting in increased costs for rate payers.

**Enbridge Additional Argument**

Pursuant to Procedural Order No.2, on November 13, 2009, Enbridge filed Additional Argument indicating a sense of urgency to implement EGD's proposed commercial Green Energy Initiatives. EGD also provided greater detail of an illustrative list of initiatives, and indicated to the Board that the time between the Minister's Directive and the filing of the application was "not sufficient for the full development of Enbridge's plans"[12]. EGD also stated that the company is not prepared to pursue some of these opportunities unless it is able to include the investments made as part of its regulated operations[13].

It seems apparent that as further submissions are made by the company outside of the Application and pre-filed evidence process that the amount of detail on various projects increases. This would indicate that these initiatives are still under development and have not been fully formulated. While this should be reason enough for the Board to deny EGD's request for these projects to be recovered from rates, the underlying principles already outlined in this argument still apply as to why these initiatives are not properly part of the regulated activities of EGD.

To address the individual projects described in EGD's Additional Argument, DE provides the following comment:

Waste energy from pressure let down stations: While this opportunity may only be available to natural gas transmitters and distributors, it should be recognized that "green" electricity would be generated by this initiative. As mentioned earlier, the Board has already set precedent in the Guidelines that these types of opportunities are not recoverable from rates. Furthermore, the production of this electricity should not be treated differently than natural gas fired power plants, in that generation fuelled by natural gas is not recoverable from distributor rates.

Solar thermal water heating: As EGD has already applied to have this program treated as a DSM initiative in its 2010 Low Income DSM Application, the grounds for also requesting cost recovery in this Application are unclear.

Capture of biogas: Previously, biogas has been viewed as a renewable resource in the production of electricity. EGD has instead suggested that biogas from its proposed facilities be injected into the natural gas distribution system for burner tip consumption. It would seem in this case, that EGD is requesting ratepayers fund the assets which would allow EGD to sell biogas back to the ratepayer as fuel. This would not only allow EGD to "double dip" from ratepayers, but would in effect make EGD a producer of natural/biogas. As the production of gas is not part of the sale, distribution, transmission and storage of gas, it should be deemed outside of the company's regulated operations.

District energy projects: EGD mentions on page 5 of its Additional Argument that "There would be no natural gas system to the community…" where District Energy projects exist. As mentioned earlier in this submission, district energy projects are not an extension of the natural gas distribution system and therefore clearly outside of the regulated operations of EGD.

While providing greater detail in its Additional Argument on some of the Green Energy Initiatives proposed by the company, EGD has not provided any evidence to demonstrate the urgency of these

[12] Enbridge Additional Submission, November 13,2009; page 2
[13] Enbridge Additional Submission, November 13,2009; pages 4, 6

projects. Furthermore, the additional details do not change the commercial nature of these projects, nor change the underlying principles as to why costs should not be recovered from rates.

**Conclusion**

In closing, it should be noted that the Board's decision in this case will be a turning point for the Ontario market. If the Board determines that it has the jurisdiction to rule on cost recovery for green energy projects and/or ultimately allow the costs of such projects to be recovered from rate base, it will pose a competitive disadvantage to private sector providers of small scale generation. It will also ensure that ratepayers will not only fund, but assume all of the risk of the implementation, maintenance and obsolescence of these assets. Furthermore, unlike DSM and CDM initiatives whereby the individual customers assume ownership of the physical and financial benefits of these programs, ratepayers will inappropriately be funding the private ownership of these assets on behalf of Enbridge shareholders.

For the reasons noted above, DE submits that the costs, assets, and revenues associated with EGD's proposed Green Energy Initiatives are not properly part of the regulated operations of Enbridge; and are therefore outside of the Board's rate making authority. It is clear that the Board has already set precedent in these matters with respect to electricity LDC's in the Guidelines issued in EB-2009-0300 which have definitively determined that such projects should be conducted outside of rate base. Furthermore, the Board has noted in the Guidelines that the current statutory framework does not permit the Board to include rate recovery for the assets, operations, and maintenance of such projects. DE believes that no foundation exists to apply different treatment to natural gas utility projects of a similar nature.