# ONTARIO ENERGY BOARD

## Demand Side Management (DSM) Guidelines for Natural Gas Utilities

## Issues for Further Comment

## Comments of Industrial Gas Users Association (IGUA)

1. By notice dated March 29, 2011 (Notice), the Board has informed stakeholders of the Board's views and considerations regarding the role of ratepayer funded DSM activities for the next three years, and has invited written comments on specific issues relating to the role of ratepayer funded DSM for that period.

2. In these comments, IGUA focuses on the question of what DSM programs, if any, are appropriate in today's market context for industrial gas customers. In these comments "**industrial**" gas customers are those whose gas consumption is process driven (rather than heat sensitive), and is thus at a high load factor.[1] This characterization of "industrial" also tends to identify those gas customers for whom gas input costs are material enough to justify dedicated internal energy management resources, and thus support an in-house sophistication and self-sufficiency when it comes to energy use and energy management decisions.

3. **It is IGUA's view that ratepayer funded DSM programs for industrial customers should be discontinued.**

### Evolution of the Energy Services Market

4. The broader process which has generated this most recent Board Notice was commenced in October, 2008. This broader process was in turn struck to consider revisions to the multi-year DSM framework initially adopted by the

[1] These customers would generally (though not exclusively) fall within Union's T1 and Rate 100 rate classes, and Enbridge's Rate 115 rate class.

Board in 2006 (EB-2006-0021). The initial multi-year framework was based on DSM guidelines established by the Board in July, 1993 (E.B.O. 169-III).

5. The DSM plans that will be informed by the views and considerations reflected in, and responses to the questions posed in, the Board's most recent Notice will be implemented for January 2012. The framework thus developed will commence nearly two decades following establishment in 2003 of the basis for the initial DSM framework.

6. IGUA agrees with the Board's observations regarding the changes that have occurred over these last two decades. In particular:

   a. The landscape for conservation has developed into one in which a much larger number of private and public entities deliver energy efficiency programs.

   b. An array of energy efficiency solutions that are economically attractive to consumers without ratepayer funded subsidies are currently available.

   c. Higher mandatory efficiency standards for new building construction and major appliances, including water heaters and furnaces, have led, and are expected to continue to lead, to significant natural gas savings over time.

   d. Governments around the globe have "got religion" on climate change concerns. As a result energy use and efficiency has become a major focus for government policy and related government programs. Canada and Ontario are no exception. Ontario energy consumers are subject to government environmental, fiscal, and social policies and programs that include a keen focus on energy use reduction.

7. In light of these changes and current market conditions, incremental benefits through ratepayer funded DSM programs will be more limited and, by necessity, more costly to implement.

8. The most recent significant contextual change relevant to considering the future of ratepayer funded DSM in Ontario was the passage of the Ontario *Green Energy and Green Economy Act, 2009* (*GEGEA*). From an industrial perspective, a main result of *GEGEA* is to increase the social program costs that will be borne by industrial energy consumers.

9. In particular:

a. Increasing costs for green electricity and electricity demand reduction and demand shifting programs have been, and will continue to be, socialized through the electricity market "global adjustment" recovered from all electricity consumers.

b. The costs of redevelopment and expansion of Ontario's electricity transmission and distribution infrastructure to connect renewable electricity generation, including "smart grid" costs, will be included in electricity rates for all electricity consumers.

c. Increasing costs for government and MUSH sector green building and procurement initiatives will be recovered through tax revenues.[2]

d. Building envelope and appliance energy efficiency standards[3] and associated costs will increase.

10. Further, the future impacts of Ontario carbon abatement legislation are not yet clear, but will in all likelihood include increased industrial sector costs.

11. These various cost pressures have culminated at a time when the rising Canadian dollar is putting upward pressure on industrial input costs, and the aftershocks of the recent global economic depression continue to be felt in financial and capital markets, and by companies making decisions about whether they can invest in new plant and products, and if so where. Both the absolute value of, and the trend in, energy costs are significant factors for industrial investment decisions.

**The Role of Economic Regulation**

12. As noted in the Board's recent Notice, the core business of natural gas distributors, and that for which the Board makes orders approving or fixing just and reasonable rates, is *"the transmission, distribution and storage of gas"*.

13. The purpose of economic regulation, the main function of the Board, is to replace market forces in the context of a network industry in which there are no

[2] *GEGEA* sections 5 through 9.
[3] *GEGEA* section 14.

competitive pressures to control price and maintain quality of customer service. A corollary of this basic premise is that where markets are functioning, the market should be left to determine the appropriate economic balance between cost and value to consumers.

14. In the current context of an array of energy management solutions that are economically attractive to consumers, the Board has expressed a concern that ratepayer funded DSM programs may have the unwanted effect of discouraging or impairing the penetration of market-driven energy solutions. IGUA agrees with this concern. Centralized regulator or utility energy solutions decisions could displace market based determinations, resulting in sub-optimal choices in the long-run. While perhaps inevitable where centralized decision making is required, such should be avoided where a robust market exists in which competing options are subject to market disciplines and determinations.

15. Other factors making rate-payer funded utility DSM programs problematic in a market place rife with energy efficiency options include:

    a. Increasingly intractable problems of identifying and quantifying free ridership effects.

    b. A potentially even more intractable problem of conclusively identifying spill over effects.

    c. Defensible attribution of benefits to competing program providers. (Agreements by utilities to "divvy up" the associated energy savings and resulting rate-payer funded shareholder incentives is, from IGUA's perspective, a less than satisfactory solution to this issue.)

16. These considerations suggest that where a robust market for energy solutions exists, there is a limited role for regulated (in this context rate-payer funded) DSM solutions.

17. IGUA acknowledges that a letter from the Ontario Minister of Energy to the Chair of the Board (dated July 5, 2010) requests that the Board *"consider expanding … general natural gas DSM efforts…"*. The context for this request is important:

a. The letter in which the Minister included this request is, with the exception of this particular passage, a letter expressly addressing low-income energy programs.

b. The Minister's request is expressly tempered by a direction to ensure *"the balancing of ratepayer interests"*. IGUA reads this reference to "balance" to direct consideration of the costs relative to the benefits of expanded DSM. The Board's observations in the Notice and the additional observations referenced above regarding the current energy services market context are directly relevant in this respect.

18. Also of relevance to consideration of the Minister's letter is the distinction between government and regulatory policy. IGUA addressed this distinction in earlier submissions in this process in the following terms:[4]

> *In the specific context of considering the Ontario government's current "green energy" policies, the Ontario Energy Board's Chair has recently articulated the distinction between regulatory policy and government policy as follows:*
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> > *Regulatory policy differs from government policy. Regulatory policy expresses the Board's independent approach to the implementation of the law and best aligns the government's policy priorities, the sector's delivery of those priorities and the protection of ratepayer interests. [Howard I. Wetston, Q.C., Speech to TransCanada Corporation MarketView, Montréal, Quebec, May 19, 2010]*
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> *The Green Energy and Green Economy Act, 2009 amended the Board's objectives in relation to gas to expressly add as an objective "the promotion of energy conservation and energy efficiency in accordance with the policies of the Government of Ontario". IGUA submits that "promotion…in accord" with government policy is quite distinct from assuming responsibility for <u>achievement</u> of government policy.* [Emphasis in original.]

19. IGUA submits that the Minister's reference to *"the balancing of ratepayer interests"* reflects (properly) a deference to this distinction between the policy role of government and that of the Board.

20. The Minister also references in his letter *"other leading jurisdictions"* as relevant to the Board's DSM considerations. IGUA's members are familiar with a number of jurisdictions in which industrial energy consumers are either excluded from, or

[4] Macleod Dixon letter dated June 8, 2010, offering IGUA's comments on the Concentric Report dated March 19, 2010.

are permitted to opt-out of, utility funded energy efficiency or green energy programs. Given the timing and cost eligibility parameters for these submissions IGUA has not conducted a comprehensive review of such practices in other jurisdictions. By way of example, however, IGUA notes the following:

a. Kentucky legislation [Ky. Rev. Stat. Ann. § 278.285(3)] allows individual industrial customers with energy intensive processes to be exempt from assignment of utility demand-side management costs if the customer implements its own energy efficiency measures

b. Legislation in Virginia [Va. Code Ann. § 56-585.1 and 56-597] excludes large (10 MW) electricity customers and excludes large commercial and large industrial gas customers from utility conservation plans and associated lost revenue adjustments, and provides for opt-out from electricity conservation plans and associated lost revenue adjustments by large general service customers who have implemented their own energy efficiency initiatives.

c. Legislation in Minnesota [Minn. Stat. § 216B.241, Subdivision 1a, paragraph b] provides that large electric customers may petition the commissioner to exempt both electric and gas utilities serving the customer from utility energy conservation charges, on the basis of evidence relating to competitive or economic pressures on the customer and a demonstration of reasonable efforts to identify, evaluate, and implement cost-effective conservation improvements at the customer's facility.

d. In Utah [Utah Code ann. § 54-7-12.6] customers that implement electricity demand-side management measures at their own expense have the opportunity to request a credit against utility demand side management charges.

e. In North Carolina [North Carolina General Statutes § 62-133.9, section (f)], industrial and large commercial customers who have or will implement demand-side management initiatives at their own expense are excluded from assignment of cost recovery for electric utility demand-side management and energy efficiency measures.

f. The Public Service Commission of South Carolina [Order No. 2010-472, July 15, 2010] approved SCE&G's proposed DSM program, which includes an opt-out from charges for the utility's program, including lost revenue adjustment and shareholder incentive components, for large customers who have already implemented or will be implementing alternative DSM programs.

g. The Corporation Commission of the State of Oklahoma [Order No. 573419, February 10, 2010] approved provisions for opt-out from Oklahoma Gas and Electric Company's electricity demand programs, for customers using more than 15 mWhs of electricity annually.

h. Duke Energy Indiana Inc. has an approved retail electric tariff effective December 1, 2010 which provides that commercial and industrial customers with annual billed peak demand greater than 500 kilowatts will not be billed for demand side management cost recovery by the utility.

**Response to Board Questions**

21. In the balance of these comments IGUA responds to those of the Board's questions of particular relevance to industrial gas consumers.

*Do industrial and commercial DSM programs with significant incentives create competitive advantages for the participants of the programs relative to their competitors?*

22. Yes, they can.

23. Properly devised DSM programs should require material customer contributions.

24. Particularly in recent economic circumstances facing Ontario's industrial sector, capital for allocation among competing internal priorities is scarce. It is those industrial energy consumers with the least amount of available internal capital to contribute to energy efficiency improvements of their own that would be most disadvantaged by being forced through levies included in regulated gas delivery rates to contribute to investments being made by their competitors, which investments would in turn reduce their competitors' costs.

25. On the other hand, when energy inputs are among the largest of a businesses' costs, the business is already fully and independently motivated to undertake economically optimal (within the broader context of its own business priorities and economics) energy efficiency investments, without the need for ratepayer funded incentives. Where ratepayer funded incentives are used, it is thus quite

possible that either the investment itself is less than economically optimal, or the incentive recipient is a free rider. Either way, ratepayer funds are quite possibly misapplied, increasing energy costs for the industrial class as a whole.

26. Unlike in the context of electricity demand reductions, where it can be argued that reduced peak demand reduces marginal costs for all users, in a continental gas market reduced use at the margin does not generally reduce landed gas costs. Gas cost benefits from DSM accrue only to those users whose gas consumption is reduced.

27. As has been previously argued by IGUA[5], real and significant expenditures have been incurred by industrial gas and electricity consumers to enhance the energy efficiency of their plant and processes. These significant early investments have been made both for the sake of environmental stewardship (and future likely legislative requirements associated therewith) and in order to remain globally competitive. It is anti-competitive to require these early adopters to additionally fund their competitors who may be choosing now to follow suit.

*What programs, if any, are appropriate for these [industrial and commercial] sectors?*

28. It is IGUA's view is that ratepayer funded DSM programs for industrial customers should be discontinued at this time.

29. However, to the extent that the Board deems it appropriate to continue to allow for some industrial ratepayer funded DSM programming, IGUA submits that such programs should be focussed on the provision of information rather than financial incentives. Further to the preceding discussion on the negative competitive impact of incentive based industrial DSM programs, any continuing DSM programming should focus on facilitation, rather than incenting, of industrial energy efficiency.

[5] Macleod Dixon letter dated June 8, 2010, offering IGUA's comments on the Concentric Report dated March 19, 2010.

30. To the extent that they are allowed to continue, ratepayer funded DSM programs for industrial customers should be focussed on energy audits and efficiency training or case studies to highlight best practices and new technologies, rather than on financing equipment and installation costs for specific DSM projects.

31. This approach will also preclude the unwanted effect of discouraging or impairing the penetration of market-driven energy solutions. Generally, DSM education and training programs and R&D initiatives and pilot programs would be least likely to disrupt "natural selection" in the market of the most effective and consumer desired energy services.

*Should the current low-income budget funding from the residential class be maintained or should the funding be recovered from all rate classes?*

32. IGUA submits that low-income DSM program funding recovery should <u>not</u> be expanded to non-residential rate classes.

33. Low-income DSM programs are, at their root, social programs. This characterization is supported by the Board's consideration of the non-energy cost benefits (such as comfort, health and general well being) incorporated into low-income DSM program screening, approval and funding determinations, in addition to empirical cost/benefit tests.

34. IGUA has consistently objected to the inclusion in regulated delivery rates of the costs of social programs, on the basis that:

   a. Such inclusion skews energy costs and thus the economic efficiency of energy choices.

   b. Social programs are the purview of government, not the economic energy regulator, and should be developed, instituted, and defended in the context of transparant democratic processess, and funded from general government revenues.

35. In the industrial and commercial context in particular, funding of social programs through regulated energy rates skews corporate choices regarding investment and location of plant and associated jobs.

36. To the extent that low-income DSM programs continue to be funded through regulated energy delivery rates, funding for these programs should continue to be recovered form residential customers. This will avoid skewing the economic decision making of commercial and inustrial customers to the detriment of Ontario's economic development policy imperatives.

37. IGUA further notes that it has, to date, had limited involvement in considerations by stakeholders and deliberations by this Board regarding low-income DSM programming.[6] To the extent that IGUA's members become responsible for funding of low-income DSM programming, IGUA will be compelled going forward to take a more active role in consultations and deliberations regarding low-income DSM programming.

38. To the extent that the Board determines to expand recovery of low-income DSM program costs beyond the residential rate class, it should also assume that future low-income program approval requests will be subject to a broader review by stakeholders, such as IGUA, who have not to date been engaged in such consultations and deliberations. In this event, the Board should assume that the process for review and approval of future low-income DSM plans will be more involved and will take more time.

**Conclusion**

39. Industrial DSM programs should be discontinued, and revenues for DSM program budgets, DSM driven lost revenue adjustments and shareholder DSM

[6] IGUA has participated on Enbridge's Evaluation and Audit Committee (EAC), and in this context IGUA's representative on that committee has been engaged in consideration of low-income DSM programming. In this role, however, IGUA's representative on Enbridge's EAC was expressly responsible for considering and advocating the interests of all ratepayers, not just industrial ratepayers.

incentives should no longer be included in determining industrial customer delivery rates.

40. In respect of those rate classes that serve exclusively high volume, process driven (high load factor) load, DSM program discontinuance can be effected simply and on a class wide basis. This would include Union rate classes 100 and T1, and Enbridge rate class 115.

41. In respect of those rate classes that combine high load factor customers with more heat sensitive customers, the Board should consider an opt out mechanism. Examples of these mechanisms have been referenced earlier in these comments, and merit more careful consideration.

ALL OF WHICH IS RESPECTFULLY SUBMITTED:

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