EB-2015-0029/0049

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sch.B, as amended;

AND IN THE MATTER OF Applications by Enbridge Gas Distribution Inc. and Union Gas Limited pursuant to the *Ontario Energy Board Act* for Orders approving their demand side management plans for the years 2015 through 2020

FINAL ARGUMENT
OF THE
SCHOOL ENERGY COALITION

October 2, 2015

JAY SHEPHERD PROFESSIONAL CORP.
2300 Yonge Street, Suite 806
Toronto, Ontario
M1P 3E5

Jay Shepherd

Tel: 416-483-3300
Fax: 416-483-3305
jay.shepherd@canadianenergylawyers.com

Counsel for the School Energy Coalition

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0 GENERAL COMMENTS

0.1 *Introduction*

0.1.1 On April 1, 2015 the Applicant Enbridge Gas Distribution and the Applicant Union Gas Limited each filed an Application for approval of a DSM plan covering the period 2015-2020 (the "Enbridge Plan" and the "Union Plan", and collectively the "Plans"). With some exceptions, the Plans make proposals consistent with the Board's "*Demand Side Management Framework for Natural Gas Distributors 2015-2020*" (the "Framework") and the related "*Filing Guidelines to the DSM Framework*" (The "Guidelines"). Those two documents, both dated December 22, 2014, set out the Board's policy with respect to Gas DSM for the period 2015-2020.

0.1.2 The Board considered the Plans by way of a joint proceeding, culminating in a lengthy oral hearing in August and September.

0.1.3 The Plans propose a total of $868 million of spending on DSM over six years, which with incentives, 15% allowed cost overruns, and lost revenue recovery, could easily total more than $1 billion over that six year period[1].

Budgets, DSMVA and Incentives 2015-2020			
($ millions)	***Enbridge***	***Union***	***Total***
Budgets			
2015	$37.722	$33.988	$71.710
2016	$63.536	$57.254	$120.790
2017	$73.827	$56.049	$129.876
2018	$79.680	$61.424	$141.104
2019	$81.274	$62.464	$143.738
2020	$82.899	$64.714	$147.613
Total Budget	$418.938	$335.893	$754.831
DSMVA (15%)	$62.841	$50.384	$113.225
Total Spend	***$481.779***	***$386.277***	***$868.056***
Shareholder Incentives			
2015	$11.090	$11.002	$22.092
2016	$10.450	$10.450	$20.900
2017	$10.450	$10.450	$20.900
2018	$10.450	$10.450	$20.900
2019	$10.450	$10.450	$20.900
2020	$10.450	$10.450	$20.900
Total to Shldr.	***$63.340***	***$63.252***	***$126.592***
Total Cost	***$545.119***	***$449.529***	***$994.648***

[1] Table takes all figures from the original Applications. LRAM is not susceptible to estimation.

0.1.4 This, combined with additional spending in CDM, is the largest expansion of conservation spending in Ontario history. If this initiative is implemented right, ratepayers will enjoy significant short and long term benefits from a forward-looking policy. If it is implemented poorly, rates will go up, and the utilities will benefit in increased profits, but the ratepayers will not.

0.1.5 The Argument-in-Chief of each of the utilities was presented orally on September 11, 2015. This is the Final Argument of the School Energy Coalition.

0.1.6 The ratepayer and environmental groups who intervened in this proceeding have worked together throughout the hearing (and on an ongoing basis in consultations and other processes prior to the hearing) to understand respective positions, hone their proposals, and avoid duplication. We have been assisted in preparing this Final Argument by that longstanding co-operation amongst parties.

0.1.7 The complexity of this proceeding necessarily required prioritization by intervenors. As a result, we have not made submissions on every issue on the Topics List, nor every sub-issue within each topic. In many cases, we have elected to focus our resources on other areas, and not develop or express positions on issues, including some that have material impacts. Where SEC indicates that it does not have submissions on any issue, that should not be interpreted as agreement with the Applications or any aspect of them, nor agreement with the position of any other party to this proceeding. Where we agree, we say so explicitly. Silence is just silence.

0.1.8 The numbering of Sections in this Final Argument is consistent with the numbering in the Topics List included by the Board in Procedural Order #1. General conclusions and recommendations have been included in this first section, which also includes a summary of more detailed positions throughout the Final Argument.

0.1.9 In this Final Argument, SEC is conscious that the policy framework surrounding the two Plans was the subject of an extensive consultation by the Board, and SEC has made its views known on the issues. While some of the same themes arise in the context of the specific Plans, SEC has attempted to ensure that it is not fighting past battles on which the Board has already reached a conclusion. Where we include positions that we have also expressed in previous submissions, it is either because we believe they are consistent with the Framework, or because there is a specific factor in one or both of the Plans that calls into question whether the Framework should be applicable to that Plan.

0.2 *Overall Theme - Expectations*

0.2.1 ***Increasing Ratepayer Commitment.*** In 2003, the combined DSM budget spend for the two gas utilities was $13.2 million[2], and the maximum shareholder incentive

[2] Union Gas $2.35 million and Enbridge $10.85 million.

available to them, collectively, was under $5 million. By 2020, the proposed budget for Enbridge is $82.9 million, and for Union is $64.7 million, in each case with a potential 15% overrun and a total of $20.9 million of available shareholder incentives between them. Thus, the total ratepayer commitment to DSM is proposed to be more than $190 million in 2020. It is a 950% increase from the 2003 total. Inflation for the same period was about 40%.

0.2.2 There is a general consensus amongst the parties, and the public, supporting the government and Board policy of increasing conservation spending. SEC and our member school boards have been conservation supporters – and implementation leaders – for many years. Our commitment has not diminished. If anything, it has grown over time.

0.2.3 ***More Money = Higher Expectations.*** But there is another side to this. With more money, and more shareholder profit, comes more responsibility. The Board will have seen that SEC's theme throughout this proceeding has been increasing the expectations placed on the utilities. In simple terms, the level of DSM performance, and approach to the DSM role, that were enough with $18 million of ratepayer money on the line is simply not enough with $190 million of ratepayer money in play. If we provide you with more money, we expect more of you.

0.2.4 The utilities have understood one part of this requirement. They are proposing to increase their CCM[3] and other metrics. While they are trying to keep the target levels down (due, they say to less low-hanging fruit, and more stringent measurement and auditing of results), they have recognized that they have to increase their results somewhat if they have a lot more money to spend.

0.2.5 What the utilities have not done is recognize that more money doesn't just mean more of the same. More money means that they have to up their game. They have to show leadership, and willingness to innovate, and higher <u>quality</u> of performance. It is not enough to increase CCM. The utilities must improve their programs and offerings, look to overcome market barriers that still remain, and reach customers that are being left behind.

0.2.6 Mr. Neme, perhaps the most authoritative voice of the witnesses the Board heard in this proceeding, talked about this in terms of willingness to take risk. Utilities are by their nature unwilling to take risk[4], but can be motivated to take risks in DSM in the right circumstances. He described it in this exchange[5]:

> *"MR. SHEPHERD: If you look at the Union and Enbridge plans that have been put forward today, and leave aside the question of whether the Board*

[3] Cumulative Cubic Metres.
[4] Tr.10:2.
[5] Tr.10:9-11.

> *is giving them enough resources to do everything they should be doing, would you say that those plans could be or should be more innovative and show more leadership than they do?*
> *MR. NEME: I think they certainly could and should, yes.*
> *MR. SHEPHERD: And can you comment on the two individual plans, in terms of the extent to which they have sufficient innovation and new thinking?*
> *MR. NEME: Well, <u>I think that both of them have room for pushing harder and farther and in newer directions</u>…*
> *MR. SHEPHERD: Now, if this Board decides to get behind an increase in innovation and a -- and require the utilities to show more leadership, there's pros and cons to that, right?*
> *I mean, on the one hand, leadership [is] a good thing, innovation is a good thing by itself. But on the other hand, that costs money and if you have a finite budget, some other things don't get done, right?*
> *MR. NEME: That's correct, and it also involves some risk. Whenever you're doing something that hasn't been tried fourteen times in the past, there is a little bit of risk.*
> *And again, that suggests that you'd want to create a framework that encourages some risk-taking that could have substantial payoffs down the road.*
> *MR. SHEPHERD: Is it fair -- in your view, is it fair to read the Conservation First concept as requiring innovation and risk-taking in conservation programs?*
> *MR. NEME: Well, let me put it this way. <u>I don't believe you can get to all cost effective efficiency if you don't take a little bit of risk.</u> It needs to be calculated risk, but I don't believe you can get there if you aren't pushing the envelope a little bit and trying new things."[emphasis added]*

0.2.7 The Ontario utilities are not taking enough risk, pushing the envelope to deliver best in class results. The Board's role should in part be to motivate them to do so.

0.2.8 This problem shows its face most clearly with the Union Gas plan, which they admit has <u>nothing</u> new in it. Nothing whatsoever[6]. It is entirely based on what they have done in the past, or tried and true programs from other jurisdictions.

0.2.9 Enbridge is not immune from this criticism. While they have proposed some newer, innovative initiatives[7], they are still taking baby steps in that direction. In SEC's submission, this is not enough.

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[6] Tr.2:152-3.
[7] See, e.g. Tr.5:148 and Tr.7:90. In general, Enbridge clearly has the mindset that they aspire to a leadership role. This is most evident when, in talking about it, the Enbridge witnesses actually start to get excited about the possibilities: see e.g. Tr.7:92-3.

0.2.10 ***Expectations.*** SEC submits that the Board should, in its decision, emphasize two key expectations of the gas utilities that, in our view, are implicit both in the Minister's Directive and in the Framework:

(a) ***Leadership.*** In developing and implementing programs and offerings, and in making both strategic and operational decisions, Enbridge and Union should at all times aim for a position of industry leadership. One key test of whether their DSM plan was successful in any given year should be whether utilities in other jurisdictions are looking to Enbridge and Union to identify leading edge, innovative, forward-thinking programs and practices. Enbridge may end up under these Plans with $550 million of ratepayer money, and Union with $450 million. The ratepayers are entitled to expect, for that, best in class performance. It is not enough to be average. They should be stellar[8].

(b) ***Impact***. Each utility should consider their receipt of this ratepayer money as a trust, in which their main goal is to use that money carefully to make a real difference. Another key test of whether their DSM plan was successful in any given year should be whether they had a real impact on the gas consumption of their customers. This is not about CCM. This is about identifying the most difficult - the highest - barriers, and then surmounting them. Over time, parties and the Board have turned DSM into an activity of "chasing the incentive", where utilities maximize their CCM through easy projects that generate shareholder incentive dollars, and eschew "the hard stuff" because it is not as lucrative. It is submitted that, with a billion dollars now on the line, it is no longer reasonable to avoid the hard stuff.

0.2.11 This is not about wanting to be proud of the programs we're funding; it is about spending to achieve something important. Ratepayers are willing to put increasing dollars into conservation, but only if those dollars are creating real, enduring change. Ratepayers are not willing simply to throw money at the problem. Ratepayers are not willing to pay more for "same old, same old". There is an opportunity here for the utilities to make real things happen, and have an important influence over gas consumption. The ratepayers have their wallets out, ready to pay for it. It is the responsibility of the utilities to deliver something that it is keeping with the price ratepayers are being asked to pay.

0.2.12 ***Board Message.*** In the best of all possible worlds, SEC believes that the Board should make a blunt, direct statement, aimed at the CEOs of Union and Enbridge, setting out the increased expectations that come from these much higher budgets. In our view, in describing how the bar is being raised, the Board should not say "Try harder". Instead, we believe the message should be "You said you wanted more money. Here it is. Now show us what you can do."

[8] We note that other jurisdictions have raised the bar successfully: Tr.10:8. There is no reason Ontario can't do the same.

0.2.13 We are conscious that we are asking a lot of the Board to make such a blunt statement. On the other hand, the utilities are asking a lot in seeking a billion dollars of ratepayer money. Which is more radical?

0.2.14 ***Shareholder Incentives***. In addition to the statement of principle, we are asking that the Board restructure the shareholder incentives, starting in 2016.

0.2.15 For each utility, we are proposing that the maximum incentive be increased to $12 million, but that it be divided into the formula component, and the discretionary component. The formula component, $8 million each per year, would follow the proposed structure. The discretionary component, on the other hand, would be up to $4 million per year awarded in whole or in part by the Board after hearing evidence by the utility that it has shown leadership, been innovative, and taken on more difficult challenges. The key would be the utility showing that they were impactful, not just quantitatively, but qualitatively as well[9].

0.2.16 ***Approvals.*** SEC is also proposing that the Board make these principles tangible by the nature of the approvals it grants.

0.2.17 With respect to Union Gas, SEC proposes that the Board reject the Plan, and require Union Gas to rollover its programs one more year, from 2015 to 2016. For the period starting in 2017, Union Gas should file a new Plan that is in keeping with the higher standard they are required to meet. In short, we are saying that the Union Plan is not salvageable in its current form.

0.2.18 With respect to Enbridge, SEC proposes that the Board give conditional approval to the Plan, with some modifications, but also require Enbridge to show, in subsequent filings, that it is expanding its programs and approach to meet this higher standard. Enbridge has started to up its game, and in our submission should be encouraged to move stronger and faster in that direction.

0.2.19 ***Conclusion***. It is somewhat ironic that SEC, which for some years has been touting the DSM work of Union and Enbridge as "great stuff", should now be saying "Not good enough." However, a billion dollars is a billion dollars, and for SEC, at least, it brings into clear focus the fact that the quality of the DSM plans for Union and Enbridge has not kept pace with the ever higher ratepayer cost of those plans[10].

0.2.20 SEC believes that the Minister's vision is not "gas conservation like everywhere else", and that should not be the Board's vision either. This Board has an opportunity to push Union and Enbridge to do what they are really capable of doing, and SEC urges the Board to take up that opportunity.

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[9] See Section 4 of this Final Argument.
[10] Mr. Neme appears to agree: see Tr. 10:7.

0.3 *The Union Plan – SEC Recommendation*

0.3.1 SEC proposes that the Board deny approval for the Union Plan, and require that they re-file with a new 2017-2020 plan, incorporating the comments in the Board's decision, by June 30, 2016. In the meantime, 2016 programs should continue using a rollover from the 2015 budgets and targets.

0.3.2 Details of SEC's criticisms of the Union Plan are found throughout this Final Argument. However, the main reasons why SEC believes the Union Plan should be rejected are the following:

(a) The Union Plan shows virtually no leadership. It contains no innovative programs or methodologies, and no attempt was made to include anything of that nature.

(b) The proposals for targets are quite obviously designed to ensure that targets will be achieved with a minimum of effort and no risk. As LPMA has pointed out, Union's targets are consistently below what they can achieve. If this happened occasionally, one could call it good performance. If it happens all the time, it is more likely under-targeting. This is exacerbated by the proposal to use 125% as the upper bound, for no other reason than 150% is "too hard".

(c) The Union Plan does not comply with the Board's guideline on ratepayer impacts, $2.00 per residential customer (about 5% of the distribution bill), and similar impacts for other customers. Properly calculated, the impact of the plan proposed is significantly higher for residential. It can be assumed that other classes are similarly affected. A typical school pays about $2,500 per year in distribution charges, but under the Union Gas proposal they would add more than 20% ($585) to the distribution bill for a typical school to pay for DSM programs (many of them for residential customers).

(d) Union seeks to return to a time when they get credit for results that are known to be incorrect, because they don't use best available information.

(e) The Union Plan continues to include ratepayer spending for Large Customer programs, even though the Board has decided against it, and even though the large customers themselves told Union that, if it were on a fee for service basis, they would not pay for it.

(f) Union has had a history of spending ratepayer money on custom projects that are plainly free riders, for example because of shockingly short payback periods. Despite this, the Union Plan continues to assume that this is appropriate behaviour. It is not.

0.3.3 Union Gas is asking the Board for authorization to charge its ratepayers $450 million to fund DSM activities. The Plan presented to the Board comes nowhere close to justifying that expenditure, and thus would not result in just and reasonable rates. In our submission, approval should be denied.

0.3.4 Having said that, SEC believes that Union should continue to offer DSM programs, and for that reason the Board should order a rollover of the 2015 budgets and targets to 2016. This will give Union time to develop a much better Plan, worthy of the money being sought, and file it with the Board by June 30, 2016 for approval. By the beginning of 2017, Union could be offering a much more sophisticated and innovative set of programs, delivering on the government's, the ratepayers', and the Board's DSM priorities.

0.4 ***The Enbridge Plan – SEC Recommendation***

0.4.1 In SEC's view Enbridge took a more thoughtful, forward-thinking approach to their Plan. While there are still lots of things that should be fixed, SEC believes that the Enbridge proposal, with the changes proposed by SEC throughout this Final Argument, can form the basis for successful achievement of the Conservation First philosophy.

0.4.2 For that reason, SEC recommends that the Board approve the Enbridge Plan, with the changes noted herein.

0.5 ***Summary of Submissions***

0.5.1 This Final Argument contains a detailed analysis of some of the issues arising in this proceeding. The following are some of the main recommendations resulting from that analysis.

0.5.2 ***"All Cost-Effective" DSM***. The Framework correctly reflects the fact that the Board does not have jurisdiction to order DSM activities that are inconsistent with just and reasonable rates. The Minister's Directive does not, and legally cannot, change that. "All cost-effective" can only mean, to be consistent with the OEB Act, all DSM that is achievable while still maintaining a level of rates that is just and reasonable. Any debate about whether the $2 per month guideline is the right level is not a DSM discussion. It is solely a discussion about reasonable rates.

0.5.3 ***Adjust 2016 Targets.*** The 2016 Union Gas targets should be adjusted in the manner described by LPMA in their Final Argument. The 2016-2020 Enbridge targets should be adjusted in the manner described in Section 2.4 below.

0.5.4 ***Annual Target Adjustments.*** Union's proposal to adjust targets for each year by reference to actual performance for the previous year should not be accepted unless it is asymmetrical. That is, the formula should increase targets to reflect higher actual performance, but should not decrease targets for the same budget levels. If that is not acceptable to the utilities, then a set of pre-determined targets until 2020, but reviewed at the mid-term review, is the appropriate approach. The ratepayers should know at least the minimum they are getting for their money, and the Board should not permit spending of ratepayer funds without knowing the minimum results that are forecast to flow from that spending.

0.5.5 ***Catchup on Scorecards.*** The impact of any individual item on a scorecard should not be less than 0%, nor more than 150%. This will help motivate the utilities to pursue all metrics, not just those that are the most successful.

0.5.6 ***Upper Bound at 150%.*** The upper bound of targets for each scorecard item should be 150% of the target for both Union and Enbridge, as set out in the Framework. The Enbridge approach in this regard is correct, and the Union proposal is simply rehashing their submissions during the formulation of the Framework.

0.5.7 ***Incent Only Real Performance – No Retroactive Adjustments.*** The two proposals to match assumptions used in targets with assumptions used for actuals should not be accepted. Those proposals focus too heavily on what is "fair" for the utilities, and not enough on what is fair for the ratepayers. Ratepayers provide money to achieve certain measured results, based on pre-agreed targets. They expect that those results will be real, and will be calculated using the best available information at all times. If the targets are changed retroactively, <u>they are not real targets</u>. If the results are measured using information that is known to be incorrect, <u>they are not real results</u>. Utilities should only be incented for meeting real targets with real results.

0.5.8 ***Union Gas Inflation Slush Fund.*** The inflation component of the Union Gas Plan should not be approved, as Union Gas has refused to advise the Board how it will be spent. The Board should not establish a new precedent of approving slush funds.

0.5.9 ***Union Gas Overall Budget.*** The proposed 2016-2020 Union Gas budgets appear to be in excess of the Board's $2 per month guideline for residential bill impacts. However, that problem can be addressed for residential by changing the residential recovery method to the monthly fixed charge, as described below. This would allow the Board to set an upper limit of $2.00 on that charge.

0.5.10 ***Benchmarking of DSM Budgets.*** The utilities should be ordered to carry out a joint benchmarking study on DSM budgets, including in particular administrative, promotion and other overhead costs. The study should be filed with their respective 2017 rate applications, in order to inform the Board whether the costs to be included in the 2017 rates are reasonable.

0.5.11 ***Disallowances of Imprudent Spending.*** The Board should give clear guidance to the utilities that, in the event that they spend ratepayer flow-through budgets imprudently, that imprudent spending can be disallowed, and the DSMVA can be used to refund that overspend to the ratepayers. Any practice of routinely incenting projects that do not need to be incented should be considered imprudent spending.

0.5.12 ***Two-Part Shareholder Incentives.*** The proposed $10.45 million shareholder incentive for each utility should be split into a maximum $8 million formula incentive and a maximum $4 million discretionary incentive for leadership, innovation, and "doing the hard stuff", as set out in more detail in Section 4. Whatever structure is provided for the shareholder incentive, SEC opposes the suggestion that all or any part of the shareholder incentive be embedded in rates. Performance-based compensation should not be paid until earned.

0.5.13 ***On-Bill Financing.*** Union Gas should be directed to explore whether it can enable on-bill financing by third parties through the Union Gas bill, in a manner similar to that already offered by Enbridge. Utility funds should not be used to provide financing for customer DSM projects. Utility funds are too expensive for that purpose.

0.5.14 ***Custom Projects Short Payback Presumption.*** Custom projects should be rebuttably presumed <u>not</u> to qualify for utility DSM programs if they have a payback of two years or less. For any given shorter payback project, the utility should be allowed to demonstrate that the project was the result of utility influence, by providing affirmative evidence as to factors that prevented the project from proceeding without the utility's expertise and/or cash contribution. Failing that proof, projects of two years or less would not be included in results, and incentives paid for those projects would not be recoverable from ratepayers.

0.5.15 ***Large Customers.*** Both utilities should be required to exit the Large Customer DSM business. Each should be allowed to have an unregulated affiliate, at their own expense, carry on a consulting service for Large Customer DSM, but it should not be funded by ratepayers.

0.5.16 ***Project Level Cost Effectiveness Testing.*** All custom projects should qualify for inclusion in utility plans only if they meet the relevant cost-effectiveness test (TRC-plus of 0.7 for low income, and 1.0 for everything else). If a project is found, under audit, to have failed the requisite test, the utility should be allowed to demonstrate that there is a separate reason to include it which justifies the spending of ratepayer funds. If the utility does not meet that onus, the project should not be included in results, nor should the amounts paid in incentives be recoverable from ratepayers.

0.5.17 ***Programs Not Cost-Effective – Residential Behavioural.*** The utilities should not have approval to proceed with their residential behavioural offerings until they are able to demonstrate that the programs are cost-effective on the TRC-plus test.

0.5.18 ***Incremental Cost-Effectiveness.*** The utilities should be required to test the size and terms of each offering or program periodically to assess whether the incremental cost of including additional terms, or expanding the size of the program, is cost-effective.

Only the cost-effective component of offerings should be implemented. Increments that are not cost-effective should not be pursued.

0.5.19 ***Avoided Costs – Cost of Carbon.*** Utility forecasts of avoided costs should include a realistic number for the actual dollar cost of carbon pricing. That number is not zero. The Board should, at the mid-term review, consider whether the 15% is the right adder in the TRC-plus test, once the cost of carbon pricing is included in avoided cost as a separate line item.

0.5.20 ***Union Gas Rates M1 and 01.*** Union Gas should be required to include the component of its DSM budgets, actual spending, shareholder incentives, and any LRAM applicable to residential programs in the fixed monthly charge for each of rates M1 and 01, to avoid the problem of commercial and industrial customers bearing a disproportionate share of residential program costs. Conversely, the commercial and industrial DSM costs included in those rate classes should be charged solely to volumetric rates, excluding the first and second blocks, so that they will be directed to higher volume customers.

0.5.21 ***DSM in Infrastructure Planning.*** The Board should take charge of developing a framework for integrating DSM and infrastructure planning. Then, it should set a deadline for the approval of utility plans to implement that framework. If there is no hard deadline, there is a danger that this will not get sufficiently high prioritization by the system planners at the utilities.

1 GUIDING PRINCIPLES AND OEB PRIORITIES

1.1 *Introduction*

1.1.1 In this section, SEC will look at certain of the guiding principles and OEB priorities. We are not considering all of them, but instead will focus on those that have generated significant disagreement and debate in their interpretation or their application to the Plans.

1.2 *"All Cost Effective" DSM*

1.2.1 The Minister's Directive to the Board[11] says:

> *"In establishing the DSM Framework, the Board shall have regard to the following objectives of the government in addition to such other factors as the Board considers appropriate:… that the DSM Framework shall enable the achievement of all cost-effective DSM."*[12]

1.2.2 The Minister's statement has led to a number of parties saying, in effect "The Minister says you've got to do it". "All cost-effective" has become, in the eyes of some, an absolute requirement driving the Board's consideration of the Plans[13].

1.2.3 With respect, the law says something quite different. The statutory power being exercised by the Board when it considers any DSM application, including the Plans in this proceeding, is in s. 36(2) of the OEB Act, which says:

> *"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."*[14]

1.2.4 While s.2 of the OEB Act sets out objectives that the Board must consider in exercising this power, and those objectives include conservation, they also include prices, as follows:

> *"2. To protect the interests of consumers with respect to prices and the reliability and quality of gas service…*
> *5. To promote energy conservation and energy efficiency in accordance with the policies of the Government of Ontario, including having regard to*

[11] O.C.467/2014. Directive of the Minister to the OEB dated March 26, 2014 (the "Directive").
[12] Directive 4(ii).
[13] See, e.g. Mr. Neme's comment at Tr.10:15 that "all cost-effective" and budget constraints are inconsistent concepts. While as a policy matter he may well be right, as a legal matter he is not.
[14] OEB Act, s. 36(2).

the consumer's economic circumstances."[15]

1.2.5 This is important because the Directive is issued under a specific section dealing with energy conservation, which states:

> *"The Minister may issue, and the Board shall implement, directives that have been approved by the Lieutenant Governor in Council that require the Board to take steps specified in the directives to promote energy conservation, energy efficiency, load management or the use of cleaner energy sources, including alternative and renewable energy sources."*[16]

1.2.6 This all probably seems pretty obvious, except that the impact may not be. The Minister's power does not extend to directing the Board to ignore Objective #2 (prices), nor to set rates that are not "just and reasonable". The Minister's power is to give direction on the implementation of Objective #5 (conservation).

1.2.7 Thus, "all cost-effective" may sound very absolute, but the Board cannot treat it as such. Indeed, the Minister could not have intended it to be absolute, since that would have been outside of the Minister's powers.

1.2.8 What is absolute is the Board's statutory mandate, which is to set just and reasonable rates. The Board does not have the authority or jurisdiction to do anything that would make rates not just and reasonable, and nothing the Minister says in the Directive can change that. Just and reasonable rates are a fundamental boundary in this proceeding, outside of which the Board cannot go. Within that boundary, the Board can and should follow the Directive, and look for utility proposals that achieve all cost-effective DSM.

1.2.9 However, if there is cost-effective DSM that is available by ignoring the protection of ratepayers as to prices, and setting rates that are not just and reasonable, the Board is legally prohibited from pursuing that additional DSM.

1.2.10 The Board has recognized the extent of its jurisdiction in the Framework, and has established a rate impact guideline designed to ensure that its primary "rates" mandate is met. One could debate whether $2 per month for a residential customer is too high or too low, but that debate would have to be entirely within the context of whether the rates are just and reasonable. That discussion is not about whether there is more DSM available. As a matter of law, that is entirely irrelevant. That discussion is, rather, solely about whether the rate impact meets the Board's statutory mandate. If it does, the Board can pursue it. If it doesn't, it can't.

1.2.11 SEC believes that some parties in this proceeding, in their desire to maximize the

[15] OEB Act, s. 2, ss. 2 and 5.
[16] OEB Act, s. 27.1(1)

DSM results for the gas utilities, and thus maximize the long term benefit to the ratepayers, have failed to take adequate account of the extent of the Board's jurisdiction, and how the Directive fits within it. There is in fact an absolute legal requirement here, but it is not "all cost-effective DSM"; it is "just and reasonable rates".

1.3 *High Customer Participation Levels*

1.3.1 The Framework provides that the utilities, in developing their Plans, should:

> ***"5. Design programs so that they achieve high customer participation levels.*** *Programs should be designed to remove financial, information and other barriers in the market place to increase take-up of DSM programs. Gas utility DSM plans should allow as many natural gas consumers as reasonably possible the opportunity to participate and share in the benefits of DSM."*[17]

1.3.2 ***Enbridge.*** SEC believes that, subject to our comments below, the Enbridge Plan seeks to achieve this for most customer groups. While there will always be some customers for whom nothing fits, Enbridge has done a pretty good job of diversity in its offerings.

1.3.3 ***Union Gas.*** The same is not true of Union Gas. SEC's biggest concern in this regard, other than our more general comment below, is that Union has not made any attempt to consider the DSM opportunities available to those who have already done a lot. After 20 years of DSM programs, and in parallel much government and industrial action on the conservation front, there are a significant minority of customers that are well along the energy efficiency path.

1.3.4 SEC considers that the Union Plan fails to make any serious effort to target the early adopters, the efficiency leaders amongst their customer base. Except to the extent that those customers are large industrials, for whom there is always another measure that can be installed every year, Union has nothing for the early adopters.

1.3.5 This is really part of the theme we have discussed elsewhere in these submissions, the problem of doing the easy stuff and avoiding the hard stuff. When a customer, like a school, or a restaurant chain, or an apartment owner, has already implemented most of the obvious efficiency measures, that is precisely when the expertise and scope of the utility can be the most valuable. For these customers, they have already said they can do the easy stuff themselves. Essentially, that's what they've done.

1.3.6 At a certain point, though, they will need help. That is exactly the wrong time for the utility to be saying "We don't need to spend time on them".

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[17] Framework, p. 8.

1.3.7 ***OPower.*** There appear to us to be two issues with the OPower program as it relates to the broad participation principle.

1.3.8 First, during the course of the hearing, it became increasingly clear that the only way any significant number of residential customers would be "participants" in DSM programs was that they would receive a letter from the utilities telling them about the OPower program. Receipt of that letter would deem them to be participants.

1.3.9 There is nothing wrong with contacting as many customers as possible, and trying to increase the mindshare they are willing to devote to energy conservation. Further, the utilities are in a difficult position on this, because they are reaching out to many customers, but almost all of those customers are passive in terms of their interaction with the utility. The point of the program is to influence behaviour without ongoing utility interaction.

1.3.10 On the other hand, treating an OPower letter recipient as a participant in the same sense as a customer that just renovated their house to make it energy efficient (under Home Reno Rebate or Home Energy Conservation) would be a stretch. In considering proposals, and data, that are driven by numbers of participants, in SEC's view the Board should treat the residential information as not being internally consistent.

1.3.11 Second, there is a different, and potentially larger, problem with the Union Behavioural offering. That offering targets the larger customers in the residential sector. That is shown in the following exchange:

> *"MR. SHEPHERD: Okay. The -- but what I'm concerned with here is that you're basically targeting your largest residential customer in the behavioural program, and that's because you think that you can get more savings from them, right?*
> *MS. BROOKS: That would be correct."*[18]

1.3.12 This is part of a lengthier exchange in which SEC noted that the average Union residential customer uses 2,583 m^3 per year[19], but the Behavioural offering targets customers that use 3,000 to 5,000 m^3 per year[20]. While it is true that those with larger homes, and higher gas use, may save more gas through behaviour change, it may also be true that the less affluent customer, with the smaller home, could be equally willing to change their behaviour, and the benefit to those customers, while smaller, could be more important to them because of their economic position.

[18] Tr.3:60.
[19] More details of the average use are provided in J3.14, which shows that the normalized average use was 2322 in 2010, and 2300 in 2014. This just makes the problem discussed above more severe.
[20] 70% of the single family residential customers, and almost 90% of the non-single family residential customers, are below this range: B.T13.Union.GEC.9.

1.3.13 This seems to us to be just another example of chasing CCM, rather than seeking an inclusive set of programs that allow everyone to participate.

1.3.14 SEC will have further comments about the OPower program later in this Final Argument. We note it at this point, though, because it would appear to us that by targeting larger customers, Union Gas is failing to pursue the guiding principle of inclusivity.

1.4 ***Co-ordination with LDCs' CDM Efforts***

1.4.1 Please see Section 11 of this Final Argument.

1.5 ***Infrastructure Planning***

1.5.1 Please see Section 12 of this Final Argument.

2 DSM TARGETS

2.1 *Introduction*

2.1.1 It goes without saying that setting targets is a key component in the expected profits of the utilities from DSM. Easier targets increase the probability that the utility will get paid all or most of their $10.45 million maximum profit level, so naturally in the Plans the proposed targets, and how they are structured, are designed to be as easy to achieve as possible.

2.1.2 This section is divided into three areas. There are some issues that are common to both utilities. Then, we deal with the separate issues that apply to Enbridge and Union.

2.2 *Overview*

2.2.1 Targets can be made easier in five ways:

(a) ***Starting point***. Whether the utility aims for 1,000 units, or 1,500 units, in a given year affects how easy it is to achieve the goal. This will apply to 2015 and 2016 for both utilities, and then will apply to 2017-2020 for Enbridge, which has specific annual targets proposed. Union has a formula.

(b) ***Target Range***. The Board has established 75% to 150% of target as the incentive range, but reducing the level for the upper bound increases the probable incentive. This issue is specific to Union.

(c) ***Annual Adjustments***. In Union's case, an annual formula to adjust targets is proposed. This is a de-risking exercise for the utility.

(d) ***Ex Post Facto Adjustments***. Enbridge has proposed a Target Adjustment Factor, which reduces targets retroactively based on new assumptions. Union has proposed a similar adjustment, but prospective only. However, they would also apply changes to actuals prospectively as well, so the result is the same.

(e) ***Scorecard Structure.*** The method of calculating target achievement, including the ability to go over 150% on a given metric, is an issue for both utilities.

2.2.2 ***Changes to Input Assumptions and Adjustment Factors***. Both utilities propose that targets and actuals be required to use the same input assumptions and adjustment factors (like free riders, persistence, etc.):

(a) Enbridge proposes to use best available information for actuals, but then apply

that same information to adjust targets using what they call the Target Adjustment Factor. For example, if in 2017 the audit of 2016 results shows that a different assumption should have been used, it is used for the 2016 actuals (and going forward), but it is also used to adjust the 2016 target retroactively to be on the same basis.

(b) Union proposes, instead, that best available information not be used for actuals that have already happened[21]. It would be used only to adjust targets and actuals on a go-forward basis. In the same example, the new assumptions in 2017 would not be applied to 2016 actuals, nor would the target be adjusted. Starting in 2017 both targets and actuals would be adjusted.

2.2.3 This is not a new debate. The issue has been debated at some length, and the Board in the 2012-2014 Framework determined that actuals should always be calculated on best available information[22]. The Board also determined that targets should not be adjusted retroactively. The current Framework does not change either of those conclusions. In fact, the Guidelines confirm that best available information has to be used for audited results, as follows[23]:

> *"The evaluation of the achieved results for the purpose of determining the lost revenue adjustment mechanism ("LRAM") amounts and the shareholder incentive amounts should be based on the best available information which, in this case, refers to the updated input assumptions resulting from the evaluation and audit process of the same program year. For example, the LRAM and shareholder incentive amounts for the 2015 program year should be based on the updated input assumptions resulting from the evaluation and audit of the 2015 results. The updates to the input assumptions resulting from the evaluation and audit of the 2015 results would likely be completed in the second half of 2016."*

2.2.4 Union, in proposing not to apply best available information to the audit of results, is flying in the face of this policy, which has stood and worked well since 2012.

2.2.5 Enbridge, on the other hand, is purporting to accept the policy, and calculate actuals based on best available information. However, it then wants to go back and adjust the targets retroactively, so that the same result is achieved as that of Union.

2.2.6 SEC discussed the philosophical problem this raises with both utilities. The concern is that the utilities look at this like they are taking a test, and they are entitled to know the

[21] See, e.g. B.T2.Union.GEC.31, which gives a specific example of how it would operate: "Any changes/updates to the input assumptions resulting from the evaluation and audit of the 2016 results would then be applied to 2016's results only for the purpose of setting the 2017 targets".
[22] EB-2008-0346 Report of the Board: DSM Guidelines for Natural Gas Utilities, June 30, 2011, p. 20. The wording is almost identical to the wording in the current Guidelines.
[23] EB-2014-0134 Guidelines, p. 25.

marking scheme in advance. The ratepayers look at this that they are paying a billion dollars, and they want to know the deliverable in advance. From the utilities point of view, it is "fairness" in the measurement of their performance. From the ratepayers point of view, it is "fairness" in getting what you paid for.

2.2.7 With Union, the question was put as follows. Note that the witnesses never actually answer the question[24]:

> *"MR. SHEPHERD: And so this is a uniquely utility-centric approach. It says this is about us; this is about what's fair to us, but I'm wondering -- and you talked to Mr. DeRose about this yesterday, but I'm wondering whether another way to approach it would be to say -- to look at it from the ratepayer point of view and say: Well, really, the target is about how much we're getting for our money, and if you change the input assumptions, that doesn't change how we're getting -- what we're getting for the money, does it?*
> *MS. LYNCH: Well, your implicit assumption there is that the input assumption is going in a negative fashion or that it's going lower, so I don't agree with your position that it's just about us. It also -- if an input assumption changes in a way that says the savings related to a particular measure or a free-rider rate is different than what we've assumed, that we would then be compensated more.*
> *MR. SHEPHERD: Your input assumptions over the last ten years have, in about 90 percent of the cases, become stricter rather than higher. That is, lower savings rather than higher savings; isn't that right?*
> *MS. LYNCH: I'd say there has been some that are lower. There are some that would be higher as well. I mean, we're also moving into new areas with new programs, so there could be other adjustments that we would see as a result of that. We're also going to be --*
> *MR. SHEPHERD: That's non-responsive.*
> *MS. LYNCH: -- more --*
> *MR. SHEPHERD: Madam Chair, this is not responsive to the question. The question is a very simple one: Do you have a lot more changes to the input assumptions that make them lower than higher over the last ten years? You can undertake if you like. I mean, we know the answer.*
> *MS. LYNCH: I'd say direction has been more down, yes, as I said."*

2.2.8 We talked about this with Enbridge witnesses as well, and they were more forthcoming[25]:

> *"MR. SHEPHERD: …And so from the ratepayers' point of view we're saying, Half-a billion dollars? We're buying 6.4 billion CCM. But you*

[24] Tr.3:16-17.
[25] Tr.5:179-81.

want to be able to say -- tell me whether this is true -- after the fact, Oh, no, no, no, you know that 6.4 billion CCM? We're changing it to 5.4 billion, but we still want the half-a billion dollars; isn't that different?
MR. LISTER: <u>Well, I think that is a bit of an oversimplification, however, directionally, or at least at a high -- in a broad sense, you're not totally inaccurate.</u>
Alternatively, if input assumptions go the other way for the same half billion, perhaps, we could produce more than 6.4 billion CCM.
MR. SHEPHERD: And how often has that happened? I asked Union the other day, and they had to admit, no, usually the input assumptions go against the utility when they're adjusted because as they get more precise they become lower; isn't that right?
MR. OTT: I'm not sure that we would characterize it necessarily as a matter of precision. I don't think you're making an unfair comment about what has historically happened…
MR. SHEPHERD: … You have a point of view on the fairness of the measurement that relates -- is a utility point of view, whether it's fair to you. I'm asking whether it is legitimate to look at it from the ratepayer's point of view as if it is a deliverable and say you've agreed to a certain deliverable, X CCM, and we gave you a certain amount of money for it, and so it's fair to us as the ratepayers that we get that deliverable and you adjust accordingly to make sure you deliver. Is that fair?
[Witness panel confers]
MR. LISTER: I think that is for the most part very in line with the proposal that we're making. So we've agreed to produce a CCM target, or being held to, as Mr. Ott called it, a meter stick, and we're simply saying that that meter stick for everybody involved, we can't -- it might change over time as a result of things that we can't -- nobody here could reasonably forecast with any degree of precision today, both sides.
So to Mr. Ott's point, you know, <u>if we go out and we accomplish that goal by replacing boilers, we still replace the boilers. They might end up being measured differently because of new input assumptions, but it doesn't change the fact that we've accomplished what we've set out to do</u>."[emphasis added]

2.2.9 In SEC's view, Enbridge falls into an obvious error here. The deliverable is not boiler replacements. The deliverable, in this example, is gas savings. That has been agreed (or ordered by the Board) in advance. It is not a good answer to say "We did all the work to get the gas savings, but they didn't actually arise."

2.2.10 In the end, this is about allocation of risk. There is a risk that a change in input assumptions or adjustment factors will make it more difficult to achieve the target metrics. The utilities want to allocate that risk to the ratepayers, by either lowering the target or pretending that more was achieved than actually was.

2.2.11 This is, in our submission, not fair to the ratepayers, and is not a reasonable allocation of the risk. The utilities are the ones in charge of their programs, and are supposed to keep up to date on the appropriate assumptions and adjustment factors affecting their programs. They have accepted targets to deliver certain results, and all activities to achieve those targets are their responsibility. Indeed, the Guidelines make clear that the utilities are supposed to keep on top of these things, for example with respect to adjustment factors[26]:

> *"The natural gas utilities should design and screen DSM programs using the best available information known to them at the relevant time, including information on adjustment factors. The natural gas utilities should continuously monitor new information and determine whether the design, delivery and set of DSM programs offered need to be adjusted based on that information."[emphasis added]*

2.2.12 SEC therefore submits that both the Enbridge Target Adjustment Factor, and the Union proposal to go back to the pre-2012 "prospective only" approach, should be rejected by the Board. As time goes on, the information on which savings calculations are made is improved. The ratepayers should not be denied the benefit of that best available information in an unfair attempt to de-risk the utility activities, and reduce their responsibility to know what they are delivering, and actually deliver it.

2.2.13 ***Scorecard Structure***. Both utilities propose to continue the current method of calculating the scorecards, such that performance can be below 0%, and above 150%, with the result that a utility can qualify for a maximum incentive while still performing poorly on some metrics.

2.2.14 SEC opposes that method of calculation. In our submission, the whole point of the4 scorecards is to ensure that the utilities pursue multiple goals, not just focus on the ones that are the easiest or most successful[27].

2.2.15 A good example is the Union Gas 2013 Low Income Scorecard[28]. Performance was calculated at 210% of the metric for single family homes (60% weight), but only 73% of the metric for multi-family homes (40% weight). The weighted total was the maximum. The poor performance on multi-family didn't matter, however, because the single-family was so high.

2.2.16 Contrast that with the situation where a scorecard weight cannot exceed the 150% maximum level. In that example, the weighted scorecard results would have been 119%, and the incentive would have been reduced. Union would still have been

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[26] Guidelines, p. 20.
[27] Indeed, for most executive and management bonus structures that use the balanced scorecard approach, performance above the maximum does not count, for exactly this reason.
[28] B.T2.Union.Staff.5, p. 3, also included in K2.4, p. 18. Discussed with Union at Tr.3:41-45.

rewarded for performing at or above the maximum level in single family, but would have lost some of their incentive due to their poor performance in multi-family.

2.2.17 SEC believes that it is appropriate to incent the utilities to redouble their efforts in areas in which they are lagging. Under the utilities' proposed calculation method, this is not necessary. In fact, it may be preferable to chase higher performance on the successful metric, and ignore the one that is proving harder to achieve.

2.2.18 This is not the response the Board should want. Multiple metrics have a purpose, and that is to ensure that multiple goals are pursued. By allowing performance in excess of the maximums to count in the same way, the purpose of the scorecard approach is undermined.

2.2.19 We have quoted the Union example above, but there are similar examples for Enbridge. We discussed this with the Enbridge witnesses as well[29]. While they note, quite fairly, that they cannot just turn programs on and off at the flick of a switch, they also agree that a 150% cap on scorecard metrics would increase their incentive to work on the stuff that is below target[30][31].

2.2.20 SEC submits that the Board should strengthen the value of the scorecard approach by requiring that no individual metric can have a "% of metric achieved" of less than 0% nor more than 150%. Below zero would be 0%, and above 150% would be 150%. The effect of this would be to put the "balanced" back into the concept of "balanced scorecard".

2.3 *Union Gas*

2.3.1 ***2015 Targets***. No submissions.

2.3.2 ***2016-2020 Targets.*** SEC has had an opportunity to review in draft form the submissions of LPMA on Union's targets for 2016 and subsequent years. Subject to our comments below, we support and adopt those submissions.

2.3.3 ***Proposed 125% Upper Bound.*** Union has proposed that the upper bound for their scorecard metrics should be 125%, rather than 150% as set out in the Framework. The Framework says[32]:

> *"In order to earn the maximum annual incentive, the gas utilities will need to meet 150% of their targets.. .[T]hree levels of achievement should be*

[29] Tr.6:8-14.
[30] Tr.6:13.
[31] Enbridge's main justification for continuing with this approach was that the Board approved it in the Framework (at page 23). What the Framework actually appears to suggest, if anything, is the opposite, but nothing turns on that. See discussion at Tr.6:10-11.
[32] Framework, p. 22-3.

provided on the scorecard(s) for each metric: one at each 75%, 100% (target), and 150%. To encourage performance beyond the 100% target level, a pivot point should be introduced at the 100% level. More specifically, 40% of the maximum shareholder incentive available (or $4.2 million) should be provided for performance achieving a scorecard weighted score of 100%, with the remaining 60% (or $6.3 million) available for performance at 150% and for achievement of targets for priority programs."[emphasis added]

2.3.4 Union is proposing, instead, the maximum incentive for performance at 125% of target. SEC specifically asked them whether this is because, in their specific situation, unlike Enbridge, the policy is not reasonably applicable to them[33]. Despite being given several opportunities, they were unwilling to say that they were a special case, so that policy was not applicable.

2.3.5 This stands to reason. Their complaint about the policy of 150% is that they only have 15% more money to pursue 50% more performance[34]. That is part of the structure of the policy. The Board contemplated exactly the situation Union is in, and decided that 150% is the right upper bound.

2.3.6 There are, however, two other reasons why the Union 125% proposal should be rejected.

2.3.7 First, their proposal is predicated on the notion that they have only the 15% DSMVA as budget to spend on the 50% uplift. That entirely misses the point. Union should be seeking to achieve their 100% target level without spending 100% of their budget, as indeed has been the case for both utilities in past years. The budget available to Union to exceed target is made up of two components:

(a) The total amount of savings achieved through efficiencies, productivity, and innovative approaches in reaching the 100% target level, and

(b) The further 15% available through the DSMVA.

2.3.8 Second, Enbridge has filed a plan that is compliant with the Board's policy, and is aiming to reach the 150% performance level. We had a discussion with them about that, specifically referencing the Union proposal of 125%[35]:

"MR. SHEPHERD: [Y]ou would agree with Union that 150 percent upper band is harder to achieve than 125 percent, especially if you only have 15 percent more money, right?

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[33] Tr.3:12-14.
[34] Tr.2:166, also at K2.4, p.15.
[35] Tr5:173-4.

MR. LISTER: Yes, I think that is intuitive and logical, that going further is more difficult.
MR. SHEPHERD: But you don't think it's impossible, do you? You don't think it's impossible to meet your upper band?
MR. LISTER: It is a difficult question, because it is projecting into the future where DSM markets might be. On a particular scorecard measure, it's happened in the past. In fact, we had a discussion earlier today about the HEC programs' success. It is not always -- <u>it's not always possible, but maybe it's never impossible.</u> So it can happen, yes.
MR. SHEPHERD: And your goal -- with the target that you've proposed -- and, I mean, we'll talk about the details of those targets. But with the targets you've proposed, your goal would still be to meet or exceed the upper band, wouldn't it?
MR. LISTER: I think that's fair. Our goal is to achieve the maximum incentive that we can achieve.
MR. SHEPHERD: And so if your staff, Ms. Oliver-Glasford, were to say to you, no, we'll never meet the CCM target; it's impossible, it's way, way too high, you're not going to say that's okay, are you?
MS. OLIVER-GLASFORD: No, I certainly would not.
MR. SHEPHERD: All right. How do you deal then with the fact that you only have 15 percent more money for a 50 percent more target? How do you manage differently to achieve the upper band with the discontinuity of funding?
MR. LISTER: Sorry, just to play your question back, are you referring to the DSMVA?
MR. SHEPHERD: Well, yeah, the DSMVA is part of it. But it's also -- I mean, you have this 50 percent --
MR. LISTER: Band, yes.
MR. SHEPHERD: -- band, yes, and you don't have 50 percent more money to chase that, right? So how do you manage differently to achieve it anyway? What do you do?
MS. OLIVER-GLASFORD: I certainly think it's going to be a challenge, and so we recognize that as a utility based on, you know, our historical and future projections.
<u>But we are going to have to be innovative about how we spend our money. We are going to have to optimize wherever possible, and collaboration may be one avenue to do that.</u>
<u>So we will be as cost effective as we possibly can moving forward</u>." [emphasis added]

2.3.9 With the greatest respect to Union, Enbridge has it right[36]. The maximum incentive is not supposed to be easy. It is supposed to be a serious, difficult challenge. It requires

[36] Although we note that the Argument in Chief seems to say otherwise: p. 14. We prefer the more motivated tone of those who have the responsibility to deliver, rather than counsel's "this is impossible" approach.

superior management decisions to achieve productivity, creativity, and innovation. That's why it's worth more than $10 million.

2.3.10 SEC therefore submits that the Union proposal to use 125% upper bound should be rejected.

2.4 ***Enbridge***

2.4.1 ***2015 Targets***. SEC is concerned that the 2015 targets for the Home Energy Conservation program have been known from the outset to be far too low to be reasonable[37]. A figure of at least 5,000 participants, and resulting CCM, would have been more sensible than the 762[38] participants. In 2016, the target is a more realistic 5,631, and even that is low (see below).

2.4.2 Enbridge's rationale for keeping the formulaic benchmark figure, even though it is obviously wrong, is that once you change one target, or one budget, to make it more realistic, you should be doing the same thing for all of them. They made an attempt to do so through stakeholdering, but they just ran out of time. To change one, but not the others, is simply not fair[39].

2.4.3 The position Enbridge is taking is not unreasonable, but it creates a problem for the Board. The Board is being asked to approve targets for 2015 that are not reasonable, and the Board knows they are not reasonable. This is not a good precedent for the Board to set. The Board should normally not approve anything that is unreasonable, no matter what the justification.

2.4.4 We do not have an easy answer to this. If 2015 were not already pretty much over, we would suggest that Enbridge be required to propose new targets, but that is obviously not realistic. They would hardly be "targets" if they are approved after the year is over.

2.4.5 Similarly, the Board could simply deem the target for this program to be equal to the actual, as a compromise. This would prevent Enbridge from earning more than 40% of the shareholder incentive for what is a very successful program. That doesn't seem fair.

2.4.6 SEC therefore concludes that the rollover target should be left as is, despite the fact that it is obviously wrong. The Board should, in its decision, make clear that it is not approving that target in the face of the evidence, but is instead allowing Enbridge to complete the full rollover, assuming that the pros and cons of doing so will even each other out.

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[37] Tr.8:101.
[38] Ex. B/1/3, p. 6.
[39] Tr.8:102.

2.4.7 SEC notes that it takes this position in large part in reliance on its submissions on catchup on the scorecards[40]. If the impact of high performance on each metric is limited to a 150% weight, as SEC proposes, then the impact of the low HEC target in 2015 is not overwhelming. Enbridge could well have performance at a 1000% level, but for scorecard purposes it would be capped at 150%.

2.4.8 Conversely, if the Board does not agree with SEC that the scorecard structure problem should be fixed, adding the 150% cap, then the low HEC target could have a significant impact on the reasonableness of the shareholder incentive. In that case, in our submission the erroneous 2015 HEC target should not be allowed to stand.

2.4.9 ***2016-2020 Targets***. SEC believes that some of the same issues that apply to the Union targets, as detailed in the LPMA submissions, also apply to Enbridge, but the problem is not as severe. SEC therefore recommends that the Enbridge targets be adjusted upwards exactly half the percentages proposed by LPMA for Union.

2.4.10 SEC is very conscious that this is not a rigorous approach to the Enbridge targets. However, after a thorough review of the evidence, we could not identify sufficient evidence to make specific adjustments on a target by target basis. There were many important issues in this proceeding, and only a very limited time to deal with them. Getting into the nuts and bolts of each proposed target would have taken more time than was available. Although the targets are very important, it was not practical to focus sufficiently on the details of each.

2.4.11 The alternative, leaving the Enbridge targets as proposed, would in our submission result in targets that are generally too easy to achieve. The small adjustment we are proposing is therefore at attempt at a compromise solution.

[40] See above, at para. 2.2.13 et seq.

3 DSM BUDGETS

3.1 *Introduction*

3.1.1 There are several specific issues relating to budgets, most of them specific to the individual utilities. Only two – benchmarking and imprudent spending – are common to both.

3.2 *Common Issue - Benchmarking*

3.2.1 ***DSM Is Not Like Other Utility Budgets.*** SEC remains very concerned with the ongoing problem of lack of accountability of utility DSM budgets. These budgets are not like other aspects of their operations, like maintenance expenses, pipe inspection, training costs, and the like. For all of those other areas, while there is usually a budget approved by the Board at the outset, utility management is then free to prioritize spending as it sees fit.

3.2.2 What that means is that the Board has to be concerned primarily with the overall spend. Management then has the responsibility to optimize the use of that money during the period rates apply, both to get maximum performance for its customers, and to earn or exceed its allowed return on equity.

3.2.3 In a rebasing, the Board looks at utility operating costs with an experienced eye. Typically there will be many years of past data available, and the number of fundamental changes in the work is very small. It is common to see a cost trajectory that is not much more than inflation, and IRM in fact assumes something less than inflation.

3.2.4 Further, to support its data-driven approach to forecast costs, the Board is turning more and more to benchmarking, both within the IRM framework and otherwise.

3.2.5 There are two important differences when it comes to DSM budgets.

3.2.6 First, they are a flow-through item. That means they are not part of the normal prioritization and optimization process of utility management. Money that is not spent is returned to the ratepayers. Overspending is – subject to some restrictions - collected from the ratepayers. Management is not free to decide that $10 million of the DSM money is better spent on pipeline integrity. It is ring-fenced.

3.2.7 Utilities like to suggest that they have made DSM part of their "core business". This is not the case, and never will be as long as the budgets for DSM are segregated in the way they are today.

3.2.8 There are good reasons why this is the case, and SEC does not suggest that ringfencing DSM budgets should be ended. However, we do believe that it is important to recognize the negative impacts of that reality, of which the most important is that management attention to ensuring productive use of the funds is reduced. Utility management is already a little distant from DSM, since it is not similar to the other things they do. The fact that they do not get to keep money they save, or apply it to other utility priorities, means they will necessarily be less driven to keep costs down. This is unavoidable.

3.2.9 While the Efficiency Carryover Mechanism helps this somewhat, by allowing the utility to seek further profits within DSM from efficiencies in spending, DSM spending will continue to be different from other spending. Money saved by efficiencies in other parts of the business goes, ultimately, to the bottom line. Money saved in DSM does not. Thus, the Board cannot count as much on management oversight of the spending to maximize productivity.

3.2.10 Second, DSM budgets relate to a specific set of programs, each of which will have its own cost drivers. While on the one hand any O&M budget for maintenance can be compared to past years' spending, and generally speaking the comparison will be a fair one, that is not true of DSM budgets. One cannot look at the budget for this year and see how it reflects a reasonable cost trajectory from past years. Changes in the programs make material differences to the budget. Top-down testing of reasonableness within the utility's own data is much more difficult.

3.2.11 This is not to say that the utilities pick their budget numbers out of the air. They do, in fact, make a concerted effort to allocate their overall budget in a thoughtful and efficient way. That, though, is an entirely bottom-up approach, and can only be tested by the Board through line by line review of the spending proposals. They are also not subject to the normal level of management review before being presented to the Board.

3.2.12 Ms. Lynch of Union described this as follows[41]:

> *"MR. SHEPHERD: In most businesses, when you take a budget forward, somebody -- senior management or whoever --has a cost effectiveness test, a sanity check, if you like -- a sanity check is the best word, where they look and they say wait a second, this is too much money, you have do this for less. Who did that this case? Anybody?*
> *MS. LYNCH: No, it's we looked at the overall budget guidance from the Board. We then looked at what the guidance was with respect to rate impacts. We took that, considered what programs we were going to offer, what we could achieve, appropriate incentive levels, and built all of that up in determining what is a plan that meets the balance of the guiding principles, key priorities, as well as the metrics as we've outlined them in the scorecard."*

[41] Tr.2:167-8.

3.2.13 We had a similar discussion with the Enbridge witnesses. They described the role of management in reviewing their proposed DSM budgets in this way[42]:

> *"MR. SHEPHERD: …While we're talking about budgets, you talked on Wednesday, somebody did, about the budget process internally, and I got the impression that there was some sort of review by management of your overall DSM budget or your residential DSM budget to see whether it was reasonable. How did that actually work? Did you -- at some point did you have to make a residential budget that you actually were willing to live with and have management push back on it? This is too much money or this is not cost effective enough? Did that happen?*
> *MR. LISTER: Not precisely like that. I think Ms. Oliver-Glasford on panel 1 described in a general sense the process…*
> *We did meet with senior management on a few occasions. We presented them with what we were going to propose to the Board. We described what the framework was after, and we described how we thought what we were going to propose met the conditions or the spirit of the framework.*
> *To say there was pushback I think maybe is not quite accurate. There were certainly questions about where this was going to go and would the Board approve levels like that, and we indicated our confidence that we were making the right proposal and the right plan, that we had the right plan.*
> *MR. SHEPHERD: And at no time did management say to you anything like, well, you know, this -- this, let's say $80 million that you want to spend in 2016, we want to spend 20 of that on something else, not DSM. They never said that? Because if the Board says you can spend 80 on DSM, they're not going to quibble with that, right?*
> *MR. LISTER: To my knowledge, management never said anything like that."[emphasis added]*

3.2.14 ***Benchmarking***. The Board has moved away from line by line budget reviews in most other areas, and instead relies on empirical analysis through benchmarking. That is the biggest single problem with the budgets presented to the Board in this proceeding. There has been no attempt whatsoever to benchmark these budgets to show the Board that the proposed spending is reasonable. Yet, without benchmarking, the Board has very little to go on in determining whether budget elements are at the right levels for the proposed results.

3.2.15 SEC pursued the issue of benchmarking with Union Gas, with a specific emphasis on the administrative costs included in the past and proposed budgets. Looking at the 2015 proposed budget of $33.988 million, the total amount to be paid out in incentives to ratepayers was $17.462 million, leaving $16.526 million for other things. Of this, $6.913 million is admin, $3.821 is promotion, $1.895 million is research and studies,

[42] Tr.8:104-106.

and the rest is mainly inflation on those items[43].

3.2.16 In the interrogatory response, Union said that they have no benchmarking information to assist in determining the reasonableness of these costs. That led to the following exchange, with reference to 2015[44]:

"MR. SHEPHERD: You have almost $7 million of administrative costs; right? About 23 percent of your budget is administrative?
MR. DIBAJI: In 2015?
MR. SHEPHERD: Yes.
MR. DIBAJI: Yes.
MR. SHEPHERD: And that goes up over time; right?
MR. DIBAJI: The percentage decreases over time, but the absolute dollars increase, yes.
MR. SHEPHERD: Exactly. And so we asked you, have you benchmarked this? You are not the only utility providing DSM programs; there's utilities all over North America providing DSM programs. They all have administrative costs. Have you made any attempt to benchmark this? And you said no, so my question is: Why not?
MR. DIBAJI: This was something we found difficult to benchmark, as different jurisdictions operate their DSM programs in different fashion. Some outsource a lot of delivery, while others have internal sales teams that outsource -- or that fall through with that delivery. Other programs have higher EM&V teams that do evaluation, so it's really hard to benchmark administration budgets and figures and compare to other utilities.
MR. SHEPHERD: Well, most of what Union Gas does is hard; that's probably not the main issue. My question is: <u>Is nobody in North America -- none of the utilities that are doing significant DSM programs, are none of them benchmarking their administrative costs?</u>
MR. DIBAJI: <u>I can't comment on that. I'm not sure.</u>
MR. SHEPHERD: Well, did you ask?
MR. DIBAJI: Did I ask if other utilities are benchmarking --
MR. SHEPHERD: Yes.
MR. DIBAJI: No, we did not ask.
MR. SHEPHERD: Did you make any enquiries whatsoever about what an appropriate level of administrative costs would be for programs of this nature?
MR. DIBAJI: Now, we assessed our past experience in delivering these programs and our administration requirements. As the teams pulled together the plans and the programs they put forward, one of the asks was to evaluate what additional administration requirements they may or may not need. In that review we optimized whatever administration funds and

[43] B.T3.Union.SEC.8, also in K2.4 as p.4-5.
[44] Tr.2:162-4.

> *people we have in our programs, and then we looked at what additional requirements we would require.*
> *MR. SHEPHERD: So you have no way of knowing whether your administrative costs are reasonable except to track them against what you've spent in the past?*
> *MR. DIBAJI: That is fair to say."[emphasis added]*

3.2.17 The same is true for Enbridge, and the same is true for all other components of the proposed spend in the Plans. Further, the number of $7 million for administrative costs for Union, in 2015, is a small portion of the overhead-related costs over the six year period of the Plans. In total, that cost, including all spending other than customer incentives, is likely at least $300 million[45], exclusive of the DSMVA.

3.2.18 Further still, we note that it is not just administrative, promotion and similar costs that could be benchmarked, but are not. Even the incentives themselves, which in many cases can be compared to similar programs in other jurisdictions, are susceptible to systematic forms of benchmarking or jurisdictional comparison.

3.2.19 SEC believes that, while the current approach to DSM budgets may have been acceptable to the Board when those budgets were much lower, the Board should not have been put in the position of approving the spending of a billion dollars of ratepayer money without thorough and complete benchmarking of the proposed spend.

3.2.20 SEC therefore proposes that any budget approval granted by the Board in this proceeding should be made on a provisional basis. Union and Enbridge should be required, on joint basis, to undertake at their own expense a benchmarking study of their proposed budgets in the Plans, both on the total spend, and on the components of their budgets. As with other DSM activities, the utilities should be encouraged to proceed with this study with active stakeholder involvement.

3.2.21 Further SEC submits that the Board should require that the joint study be filed with the 2017 IRM rate applications for the respective utilities. The Board can then determine whether the study should be considered at that time, when considering recovery in 2017 rates, or in the mid-term review, depending on the contents of the study.

3.3 *Common Issue – Imprudent Spending*

3.3.1 SEC notes that much of this hearing proceeded on the assumption that, once the budgets are approved, the utilities can spend them, and no-one will review that spending. To the extent, for example, that incentives are paid to customers that are obviously free riders, that fact might have an impact on the scorecards, and thus the shareholder incentive, but the budget amount spent will still be recovered from ratepayers. That has also usually been the assumption at Audit Committees, and in the

[45] 40% of total proposed budgets before DSMVA and shareholder incentives.

very few clearance proceedings that have been contested.

3.3.2 We are concerned about this assumption. In our view, the utilities should assume that, if the money they collect from ratepayers to fund their DSM programs is not spent prudently, they will be denied recovery of those amounts in rates.

3.3.3 In our submission, the Board should make clear in its decision that all spending on DSM, even though collected in rates through flow-through mechanisms, is still subject to after-the-fact review of prudence**.** It is the responsibility of the utility to ensure that all spending is prudent, and to answer questions in any clearance proceeding about how it has spent its budget.

3.3.4 To the best of our knowledge, this has never been done before. However, the utilities have never before had a billion dollars at their disposal for DSM, either.

3.4 *Union Gas*

3.4.1 SEC has two specific concerns about the budgets proposed by Union Gas.

3.4.2 ***The Board's Budget Guideline***. On the basis of the evidence provided to the Board, it would appear to us that the budgets proposed by Union by 2020 do not comply with the $2 per residential customer per month guidelines established by the Board in the Framework.

3.4.3 SEC pursued this issue in questioning the Union Gas witness panel[46], using the 2014 actual average residential use of 2583 m^3 per customer[47]. In a separate undertaking response to a question from SEC, Union has reported normalized average use for residential customers at 2300 m^3 per customer[48]. The unit rates for Rate M1 (Union South) for DSM costs are 1.3037 cents per m^3 , and for Rate 01 (Union North) 1.4626 cents per m^3 .[49]

3.4.4 Union has not provided separate average residential uses for North and South, but it can be seen that in both cases, applying the 2300 m^3 per customer average[50] produces a higher monthly bill impact than the Board's guideline of $2.00. For the South, the monthly cost is $2.50 ($29.99 per year), and for the North the monthly cost is $2.80 ($33.64 per year)[51].

3.4.5 Union's explanation is that they use a standard of 2200 m^3 per customer to calculate

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[46] Tr.3:83-5.
[47] B.T13.Union.GEC.9.
[48] J3.14.
[49] B.T10.Union.SEC.27.
[50] We recognize that this is likely higher in Union North, and lower in Union South, but that data is not on the record.
[51] See table in para. 10.2.6.

rate impacts. With respect, the Board did not direct the utilities to limit pretend rate impacts to $2.00 per month. If the real impact for the real average customer is $2.50 or $2.80, that is simply non-compliant with the Board's budget guideline.

3.4.6 SEC has, in Section 10.2 of this Final Argument, proposed that Union recover its residential DSM costs through a fixed amount monthly fixed charge for rate M1 and 01 customers, in order to solve the problem of intra-class subsidies between Commercial/Industrial and Residential customers in those classes. That would solve the overall problem of meeting the guidelines, because the Board could stipulate that the total charge to the residential customers could not exceed that $2.00 per month, including all components of the residential DSM budget, incentives, and other costs residential customers must bear. It would then be up to Union to ensure that its residential spending, coupled with its potential shareholder incentive, etc., did not outstrip its ability to collect from M1 and 01 customers.

3.4.7 However, SEC believes that the Board should still require Union to re-file its budgets for each year, showing that overall budget is within the Board's rate impact guidelines, not just for residential but on a proportional basis for all other customers.

3.4.8 ***Inflation Adder.*** Union has proposed that it be allowed to include in its budgets a total of almost $15 million in accumulating inflation on the amounts in its budgets[52], about 4.43% of the total budget it is requesting in this proceeding. SEC asked for details of how that $15 million was going to be spent, both in an interrogatory and during the oral hearing[53]. Union has declined to provide any details of how that will be spent, and insists that it simply have full discretion to spend it any way it sees fit[54].

3.4.9 While there may be every reason to believe that Union will in fact spend that $15 million on cost escalation, SEC is concerned that a precedent would be set here. It is not the Board's practice to authorize contingency amounts when it is considering a budget built on a cost of service basis. Utilities are expected to forecast their costs, and not build in additional amounts to allocate later in their sole discretion. That makes it difficult for the Board to determine that the proposed budget will produce just and reasonable rates. How can the Board know that, if it doesn't know how money is to be spent?

3.4.10 In this case, Union had ample opportunity to allocate this amount within its budgets, and it would not have been a difficult task. It knew the issue was live at least by the time of the interrogatories, and even in the oral hearing simply refused to provide an allocation.

3.4.11 In these circumstances, SEC believes that the Board should not approve that

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[52] B.T3.Union.SEC.28.
[53] Tr.3:2-5.
[54] Tr.3:5.

component of the Union DSM budget, in the amount of $14.978 million.

3.5 *Enbridge*

3.5.1 SEC has noted that in the Enbridge proposals, as augmented by oral evidence, certain parts of the Enbridge budget are intended to be ring-fenced. While we believe that Enbridge has agreed with this treatment, we wanted to flag them in our Final Argument so that the Board can, if it agrees, include them specifically in its decision and order.

3.5.2 ***Collaboration and Innovation Fund.*** The Enbridge proposal is that this budget, $1 million per year, be accumulated and available only for qualified collaboration and innovation activities[55]. The $1 million is included in the $4.92 million budget increase for 2015 (see below), but is a separate budget item in each subsequent year. Thus, the total is $6 million.

3.5.3 SEC has some concerns about how this fund is structured, set out in Section 5.5, but in general we strongly support the inclusion of this budget item and the purposes for which it is established. We believe, further, that the flexibility to spend it as required during the six years, rather than be limited to $1 million to be spent in each year, is a good addition.

3.5.4 SEC therefore proposes that the $6 million total CIF be ring-fenced, and Enbridge be allowed to spend all or any part of it in any year of the Plan for the stipulated purposes. By setting up this restriction, the Board would be authorizing $1 million per year of recovery from ratepayers, but would be freeing Enbridge to spend the money in any year, unrelated to the year ratepayers are paying it. For DSMVA purposes, it would be treated as spent each year, until the end of the Plan. Any unspent funds at the end of the Plan would be returned to ratepayers. Overspend would, of course, not be recoverable except through reallocations from other areas of the budget.

3.5.5 Clearly, the potential would existing for gaming this, in that Enbridge could simply sit on the money, interest-free, until the very end. However, given the purposes to which it is dedicated, and the potential benefits to Enbridge from spending it quickly and wisely, SEC is not concerned with that kind of gaming.

3.5.6 ***Excess 2015 Budget for Board Priorities.*** Enbridge added 15% to its 2015 budget, a total of $4.92 million, as allowed by the Board in the Framework, to pursue initiatives related to the Board's priorities as set out in the Framework. In the hearing, Enbridge agreed that it may not be able to spend all of that in 2015, and may not spend it on the particular initiatives in the amounts set out in the budget[56]. Enbridge agreed that it would be suitable to ring-fence this amount for the initiatives listed in the budget, but

[55] Tr.6:25.
[56] Tr.6:20-23.

allow Enbridge to spend it in either 2015 or 2016, depending how quickly the initiatives move ahead.

3.5.7 The amount of $4.92 million should be reduced by $1 million, reflecting the CIF, which would be the subject of a separate ring-fence. Of the remaining $3.92 million, the biggest component of that is costs associated with the OPower initiative. SEC has expressed separate concerns about that in Section 5.5. of this Final Argument.

3.5.8 Subject to those caveats, SEC submits that the Board should direct Enbridge to spend that extra budget on the initiatives listed, either in 2015 or 2016, as the timing is required. To the extent that the funds are not spent on those initiatives, they should be returned to the ratepayers through the DSMVA.

3.6 *Conclusions*

3.6.1 DSM Budgets have a number of unusual aspects to them. As the budgets are getting larger, ratepayers and the Board should be increasingly concerned that the budgets be assessed with the same thoroughness and rigour that is applied to other parts of the gas distribution business.

3.6.2 This section includes some specific comments relative to the two utilities, but by far the most important recommendation is that the utilities be required to benchmark their costs. That is the only way the Board will be able to have confidence that the budget levels proposed are reasonable.

4 SHAREHOLDER INCENTIVES

4.1 *General*

4.1.1 The purpose of the shareholder incentive is to focus the attention of the utility and its staff on the objectives and priorities embedded in the DSM Plan[57]. In this section, we deal with the structure of the shareholder incentive, and the proposal to embed some part of the incentive in rates.

4.2 *SEC Proposed Shareholder Incentive Model*

4.2.1 Throughout this proceeding there has been the suggestion that, as the shareholder incentive has become bigger, the utilities have been more and more motivated to "chase the incentive", which in practical terms usually means maximizing CCM.

4.2.2 In one respect, this makes some sense. The whole point of the incentive is to influence behaviour, and delivering on the metrics is the behaviour the Board and the ratepayers want to promote.

4.2.3 The problem, as we have discussed at length in Section 0.2, is that chasing the next CCM is not always consistent with developing and maintaining a leading-edge, diverse set of programs. And, it is certainly not always consistent with "getting the hard stuff".

4.2.4 To shift the focus, SEC proposes that the shareholder incentive be increased and restructured to increase the emphasis on leadership and innovation. Our proposal is the following:

(a) Increase the maximum annual shareholder incentive for each utility from $10.45 million to $12.0 million.

(b) For $8 million of the annual incentive, calculate and pay the amount earned using the scorecard and weighting method currently included in the Framework. The 100% of target pivot point would continue to be 40%, but that dollar figure would be $3.2 million instead of $4.18 million. In all other respects, the calculation would follow the same form, but with the amounts proportional.

(c) For the other $4 million of the annual incentive, pay it out only after a decision by the Board assessing the extent to which the utility has shown leadership, innovation and other attributes that are not fully measured by the formula. The

[57] Tr.3:23. This appears to be generally agreed by all parties.

discretionary component could be paid in whole or in part, but the Board would make clear that full payment would require obvious and sustained leadership at a very high level. The annual decision as to how much, if any, of this component would be paid would be at the same time as the clearance of the DSM deferral and variance accounts.

4.2.5 SEC is under no illusions that this restructuring would suddenly vault the Ontario utilities into world DSM domination. Nor, we should add, do we think that the decision whether to award any of the discretionary amount would be easy.

4.2.6 We do, however, believe that there is no formulaic way to incent innovation and leadership. These are not matters that are susceptible to number-crunching. They more often come under the category of "know it when you see it", so we do believe that a Board panel, after submissions from the parties in a proceeding, will be able to assess fairly how well the utility has done in achieving these objectives.

4.2.7 The more important aspect of this, though, is to get the utilities thinking consciously about how they will show leadership, and how they can increase their level of innovation. What we want to happen is that each utility asks itself "What can we do to maximize the amount of this leadership and innovation incentive we earn?" They are not really asking this question today, because we have not made it financially attractive to do so.

4.2.8 The utilities will, of course, argue that a broad discretion like this is not fair to them. They won't know the bar they have to clear, they will say. SEC disagrees. In fact, in most large organizations the board of directors, in addition to formulaic performance bonuses, retains a power, used periodically, to provide additional (usually called "extraordinary") bonuses when executives and other employees achieve difficult goals in an exceptional manner. Why should the utilities be any different in their DSM performance?

4.2.9 The shareholder incentive is intended to motivate the utilities to focus on the Board's, and the ratepayers', priorities. Innovation and leadership should be an important part of those priorities. Setting aside a significant component of the shareholder incentive, and making it depend on achieving those most difficult goals, is in our submission the best way the Board can ensure that it becomes top of mind.

4.3 ***Embedding the Incentive in Rates***

4.3.1 SEC does not believe that it is appropriate to embed any part of the shareholder incentive in rates, for two reasons.

4.3.2 First, it is not normal practice to pay performance-driven compensation prior to the performance on which it is based. While an exception sometimes is made for a commission salesperson who will get a small advance on their commission so that they have cash flow, that is clearly not the case here. The Applicants here do not need another $4 million a year in regular cash flow to buy groceries.

4.3.3 In the more typical case, such as executive compensation, bonuses are determined at the end of the year, and are paid when the performance that grounds the bonus has been reviewed and confirmed. If you suggested to the boards of directors of either Applicant that their executives wanted 40% of their annual bonus paid along with their salaries, they would think you were nuts. This situation is no different.

4.3.4 In our view, performance-based compensation should be paid on performance, and not before.

4.3.5 Second, there has already been some concern expressed during this proceeding that the Applicants may have developed, in varying degrees, a sense of entitlement to their shareholder incentives. We know some of the Final Arguments will refer to this, and SEC is also concerned that the mental link between performance and profit may be weakening.

4.3.6 SEC believes that embedding some of the incentive in rates may exacerbate this tendency, at exactly the time when the utilities should be asked to perform better.

4.3.7 The argument is made that this will reduce volatility. We do not see that as being the case. Since the incentive would have to be trued up by rate class in any case, there will always be changes to how much is being charged to ratepayers in a given year for DSM. The impact of embedding $4 million in rates, when some of it will be reallocated later, and the total will be changed, does not appear to us to provide a meaningful reduction in volatility.

4.3.8 For these reasons, SEC believes that the Board should not approve the embedding proposal.

5 PROGRAM TYPES

5.1 *Introduction*

5.1.1 SEC cannot comment in detail on all of the programs and offerings, but offers the following input for the Board on some of the proposals seen in this proceeding.

5.2 *Issues Common to Both Plans*

5.2.1 There are four issues that apply to both plans. The first three are included in this section, and the third is dealt with separately in Section 5.3.

5.2.2 ***Stakeholder Engagement and Successful Plans.*** The unfortunate result of the timing this year was that stakeholder engagement in plan development was done in haste, and then abruptly cut off before completion. There is no-one to blame for this, but it is an important fact in looking at the Plans.

5.2.3 SEC strongly supports the statement of Mr. Neme, where he said, referring in particular to a jurisdiction, Massachusetts, considered by many to be the North American leader in energy efficiency[58]:

> *"Jurisdictions that require pursuit of all cost-effective efficiency and <u>that involve, in an ongoing way, stakeholder engagement, not just around savings targets but around program design</u> -- and some of the New England states are classic examples of that. I believe in Massachusetts -- I may be wrong about this, but I believe that they haven't had a contested proceeding on DSM in 20 years because <u>the stakeholders are engaged in a very deliberate and intentional process upfront</u>, and they can bring through that process kind of innovative ideas, and because there is an obligation in that state, for example, for the utilities to pursue all cost-effective efficiency, they, by definition, have to kind of push themselves to the envelope a little bit."[emphasis added]*

5.2.4 ***OPower.*** We have noted elsewhere in this Final Argument that the Residential Behavioural Offering does not fare well when tested for cost-effectiveness. Until that offering can be shown to pass the TRC-plus test, in our submission the utilities should not proceed with it.

5.2.5 ***On-Bill Financing.*** A number of parties to this proceeding have suggested that the utilities incent DSM through offering to finance it on the bill[59].

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[58] Tr.10:3.
[59] We note that none of those promoting this have finance experience.

5.2.6 This is an idea that has already been explored by the utilities and their stakeholders at some length. There are two aspects to it. First, should the utilities facilitate financing of DSM through their bill, provided by third parties (with or without a buydown of the cost)? Second, should the utilities provide utility money to finance DSM?

5.2.7 ***Access to the Utility Bill.*** On the first question, Enbridge is already providing the capability for energy-related products and services, including DSM, to be billed to customers through the utility bill. This is an active and successful program, and any Enbridge customer that wants to pay for DSM initiatives on their bill has multiple options to do that. Mr. McGill, who set up that program for Enbridge some years ago, described it in this exchange[60]:

> *"MR. SHEPHERD: Okay, let me ask you briefly about on-bill financing, and most of this you dealt with, Mr. McGill. We go way back on this issue.*
> *MR. McGILL: Way back.*
> *MR. SHEPHERD: It's true, isn't it, that right now a residential ratepayer that wants to put more efficient gear in their home or put in insulation or stuff like that has a broad set of choices from contractors and financiers who will allow them to -- who will supply the stuff and finance the stuff and including a number that will put it on the bill, right?*
> *MR. MCGILL: That's correct. Yes.*
> *MR. SHEPHERD: So if I want to go out and spend $20,000 to reinsulate my home, which I did, I don't -- I'm not going to call Enbridge and say, Can you finance this, because I've got lots of people who will finance this.*
> *MR. McGILL: That's correct, and I think, given the evolution of the unbundled utility we have now, I think the company has, in some respects, encouraged customers to look elsewhere for that kind of --*
> *MR. SHEPHERD: And -- but the other side is, if I want to spend that $20,000, you might buy down the cost of that, either the cost of the financing or the cost of the gear, you might write a cheque, in fact, you do, right, for $2,500.*
> *MR. McGILL: In some programs, yes.*
> *MR. SHEPHERD: And it doesn't matter to me, as a consumer, whether you are buying down the interest rate on my financing or you are writing me a cheque as an incentive for the gear, it's still the same dollars; right?*
> *MR. McGILL: I would think that most consumers are considering the end cost to them, and they're probably -- I would agree that they're probably less concerned with the structuring of how that cost is presented to them."*
> *[emphasis added]*

5.2.8 SEC submits that Enbridge is delivering exactly the solution that is needed, tapping competitive funds already available in the marketplace, and maintaining an appropriate role as facilitator. This is done at low cost (net gain to the ratepayers, actually), and

[60] Tr.8:106.

supports the DSM activities of the company. In short, it works. Anyone who wants to finance on the bill, and has appropriate credit, can do so.

5.2.9 Union has not made such a facility available, and did not explore whether that would be appropriate[61]. In our submission, Union should do so, building on the extensive experience of Enbridge, and tapping the financiers and contractors in their franchise area as partners.

5.2.10 ***Use of Utility Funds.*** Some parties argue that the utility should actually be the financier of these initiatives, providing the money and taking the credit risk. The theory is that the utility has access to inexpensive funds, and can lend to those who would not otherwise qualify for commercial credit.

5.2.11 Both of these justifications are incorrect.

5.2.12 With respect to the utilities' cost of funds, in a regulatory environment utilities actually "pay" (that is, their ratepayers pay) a total weighted average cost of capital, plus taxes, of almost 8% today. This is cheaper than many credit cards, but more expensive than the cost of funds of almost any other financier. On top of that are the costs to manage a loan portfolio. Most creditworthy utility customers can access funds at a lower retail rate than that through their banks and other regular relationships.

5.2.13 Utilities are not able to provide financing cheaper than the private sector. This is no surprise. Financiers are in the business of providing financing. Of course they are going to be able to do it more efficiently than a gas utility, whose core business is something else.

5.2.14 The other question is whether utility financing should be provided to customers that otherwise don't qualify for commercial financing in the market. The resounding answer is no. Canada already has a problem with excessive consumer debt. The last thing that is in the public interest is for utilities, who have no experience with assessing creditworthiness, to increase the indebtedness of people who don't qualify for more borrowing. Should utilities be inviting people who are already overextended to borrow more? Likely not.

5.2.15 In our submission, direct action by utilities to get into the financing business is a very bad idea. Thankfully, the utilities have already determined that, and in our submission the Board should agree.

5.3 ***Custom Projects and the Obvious Free Rider***

5.3.1 Both utilities get a large percentage of their CCM results, and large part of their shareholder incentive, from custom projects for commercial, industrial, and multi-

[61] Tr.2:157.

residential customers. Many of these projects are characterized by very short paybacks, often under two years, but in many cases measured in months or weeks[62].

5.3.2 What can be seen, for example, is that for the commercial/industrial custom projects sampled for engineering review[63], five of the 19 had paybacks under two years, and the average for all of them was 6 years.

5.3.3 For the large volume projects (most of which are T1) sampled[64], 19 out of the 23 listed had paybacks under two years, and the average for all of the projects was ten months[65]. For those subset of projects, Union in 2013 claimed more than 1 billion CCM of savings[66]. Union calculated that the incremental shareholder incentive due to just those projects with under one year payback (15 of the 23) was $1,150,000[67], even though the total incentives paid to the customers for those projects was only $560,796[68].

5.3.4 SEC submits that this is not appropriate. Projects that have very short paybacks should raise a red flag for the utility that they do not need to spend ratepayer money to make the project happen. In most of these cases, the short payback will be sufficient for sophisticated customers, acting rationally, to implement the projects.

5.3.5 While SEC focused on Union, which has the bigger problem in this regard, Enbridge has the same issue on a smaller scale. Enbridge also incents projects that are obvious free riders. It just has fewer customers who would be in that category.

5.3.6 To solve this problem, SEC believes the Board should establish a rule that custom projects with a simple payback of two years or less should be rebuttably presumed to be disqualified from program participation. In the unique case in which there is a short payback, but there are other reasons why the project will not go ahead without utility support (a new technology, for example), the utility should be able to show, by direct evidence, that the project would not have proceeded otherwise.

5.3.7 SEC believes that the vast majority of projects with paybacks under two years will go ahead without the utility, because the economics are compelling. However, it is important to make the presumption rebuttable, so that utilities don't lose short payback projects that really do need their help.

5.3.8 We also note that this is an opportune time to implement this rule. A net to gross study for custom projects is just about to start. The current free rider assumption for

[62] See, for example, K2.4, pages 28 and 30, which are excerpts from B.T5.Union.Staff.16.
[63] K2.4, p. 28.
[64] K2.4, p. 30.
[65] Tr.3:37.
[66] Tr.3:40.
[67] J3.4.
[68] $780,013, less $219,217 incentives paid on the 8 projects over one year.

custom projects is 50%, which may in part be due to the inclusion of these short payback projects that would go ahead anyway. This short payback rule will likely have a material downward impact on the free ridership assumption for custom projects, and so now is the time to put it in place.

5.3.9 We note that exclusion of short payback projects is not a new idea. As Mr. Woolf from Synapse confirmed, it is "common practice"[69]**.** In our submission, this would be a good step to ensure, in Ontario, that ratepayer funds are focused on the projects where they are really needed.

5.4 *Union Gas Proposals*

5.4.1 This section includes a series of brief (i.e. time constrained) comments on some of the Union Gas program proposals. We have not repeated here our significant criticisms of lack of innovation and leadership, discussed earlier.

5.4.2 ***Programs for Schools.*** Union admits that school boards, the members of the School Energy Coalition, are often ahead of the curve when it comes to energy conservation measures[70]. Notwithstanding that, their offerings available to schools are mostly limited to prescriptive measures[71], which will of course exclude the most innovative options schools could consider[72]. Asked about the Energy Leaders program being proposed by Enbridge, Union said they have not considered anything like that.

5.4.3 In our submission, a comprehensive set of DSM offerings should not exclude the customers who are ahead of the curve, or deliberately limit the options available to them. Certainly, getting incremental savings from buildings like schools that already have implemented many conservation initiatives is more difficult, but that is not a reason not to do it.

5.4.4 SEC submits that, if Union is required to re-file their Plan, they should be required to include specific programs directed at customers who are early adopters or have otherwise moved ahead of the curve, but still have savings potential available.

5.4.5 ***Home Reno Rebate.*** We are aware that other parties will be providing more detailed submissions on Home Reno Rebate, so we will limit our submissions to two items.

5.4.6 Union has proposed two main changes to the Home Reno Rebate offering. First, they want to reduce the 25% savings requirement to 15%, and second they want to remove the cap on the incentive per customer.

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[69] Tr.12:67.
[70] Tr.3:76.
[71] Tr.3:75.
[72] Prescriptive measures are generally reserved for well-known technologies that have good market availability and do not need custom thinking.

5.4.7 SEC submits that the reduction from 25% to 15% seems mostly driven by the desire to make achieving metrics more easily. Unless the targets are substantially increased beyond those that are proposed, SEC believes this reduction is inappropriate.

5.4.8 The increase in the maximum incentive is a different story. Paying more should increase results, but given the popularity of these offerings at both utilities, it is questionable whether higher spending per participant is required for success.

5.4.9 However, if the real intent is to increase the savings per participant, by causing them to implement more eligible measures than the minimum two, SEC believes that is a valuable goal.

5.4.10 To achieve that result, SEC proposes that the cap be increased as proposed by Union, but only for participants that implement at least four eligible measures. This will focus the additional spending where needed, and not simply give more money to those customers for whom the existing incentive is enough. In any case, it is likely that the customers who would qualify for the additional funds would be the four or more measure participants anyway, meaning that a Board direction requiring that criterion would not materially change the outcome.

5.4.11 ***Large Users.*** There has been considerable controversy in this proceeding about Union's proposal to continue offering DSM programs to large users.

5.4.12 SEC has read the submissions of CME in draft, and the submissions of IGUA, both of whom represent large users, and both of whom oppose the continuation of the large user offering. SEC agrees with those submissions, and recommends that the Board order Union to cease offering DSM programs to large users using ratepayer funds.

5.4.13 ***No Studies of Energy Intensity.*** SEC was surprised to learn that Union has not done a detailed investigation of customer energy intensity[73]. From 2010 to 2014, and despite all of the many millions of dollars spent on residential conservation (by Union, by OPA, by governments, and by others), the average use per residential customer has actually increased by 14.5%, and on a weather normalized basis has only decreased by less than 1%[74].

5.4.14 In our submission, good program design requires thorough and complete customer data. It was clear from our discussion with Union witnesses that, if the company has that data, the DSM group certainly is not using it.

5.4.15 SEC submits that the Board should encourage Union to gather detailed data on customer energy intensity and uses, and apply that data in its DSM program design.

[73] Tr.3:81.
[74] J3.14.

5.5 *Enbridge Proposals*

5.5.1 SEC has only two minor comments on the Enbridge program proposals.

5.5.2 ***Energy Leaders.*** SEC believes that Energy Leaders has the potential to be a very good program, but notes with dismay that it is not actually a real offering with a real budget, but is more a marketing initiative[75]. Further, no-one is assigned to have responsibility for it[76].

5.5.3 It may be that these two facts are not problematic, and that Energy Leaders will become a valuable part of the Enbridge portfolio. We are concerned, however, that it not get lost because of its unique nature.

5.5.4 To that end, we believe the Board should expressly support the innovative nature of the Energy Leaders offering, and encourage Enbridge to turn it into a full-scale program with budget and adequate resources.

5.5.5 ***Collaboration and Innovation Fund.*** SEC is also supportive of the Collaboration and Innovation Fund, but notes that, as envisioned in practice, Enbridge will use this almost exclusively for collaboration[77]. While collaboration is certainly important, SEC believes that a focus on innovation would yield even greater benefits.

5.5.6 That having been said, SEC has proposed elsewhere in this Final Argument that the shareholder incentive be divided into two components, one of which is directly targeted at leadership and innovation. If the Board accepts that recommendation, then we believe the CIF may well have more focus on innovation, as Enbridge seeks to maximize its discretionary shareholder incentive.

[75] Tr.5:151.
[76] Tr.5:153.
[77] Tr.5:158.

6 PROGRAM EVALUATION (INCLUDING ADJUSTMENT FACTORS)

No submissions.

7 INPUT ASSUMPTIONS

7.1 *General*

7.1.1 The process of development and promulgation of input assumptions (which in this context includes the adjustment factors, such as net to gross, persistence, etc.) has been carried out by the utilities, with the assistance of the TEC, for the last three years. The Board is now transitioning that activity to the new Evaluation Advisory Committee. As SEC understands it, neither of the Applicants is seeking approval for any input assumptions (other than avoided costs, which are in the broadest sense a type of input assumption) in this proceeding that have not been approved by the TEC, or by previous processes. The input assumptions proposed are the existing assumptions, without amendment.

7.1.2 SEC therefore has no submissions with respect to the basic set of input assumptions on which the Plans are based.

7.1.3 That leaves two other related questions: the process for changing input assumptions going forward, and the method by which changing input assumptions are applied to actuals and targets.

7.1.4 On the first question, the process going forward, the Board has announced the formation of a new committee, and is moving in a new direction, under the more direct supervision of Board staff. SEC has expressed its grave concerns about this direction, but the Board has made a policy determination, and SEC is committed to assisting, to the extent possible, to make that new direction work.

7.1.5 On the second question, we have included our submissions on that point in Section 2.2 of this Final Argument.

8 COST EFFECTIVENESS SCREENING

8.1 *Introduction*

8.1.1 There are many issues associated with cost-effectiveness testing by Enbridge and Union, but in this Final Argument SEC will only focus on two of them: incremental cost-effectiveness testing, and individual project/program screening.

8.2 *Portfolio vs. Program vs. Project Screening*

8.2.1 There are three components to the issue of program or project cost-effectiveness:

(a) Projects that are not cost-effective;

(b) Programs with low TRC ratios;

(c) Projects with very short paybacks.

8.2.2 ***Individual Projects Not Cost-Effective.*** Union had two 2013 low income custom projects that had paybacks of 295 years and 436 years[78] respectively. These projects are clearly not cost effective. Indeed, the paybacks are shocking, since the buildings will not be around long enough to get any real benefit from the projects[79].

8.2.3 When we asked Union about these projects, they said that the reason they were incented by the ratepayers is that the customers were seeking other goals, namely comfort, and that was the primary driver for the projects[80]. The projects are not justified on the basis of energy savings at all. The energy savings are marginal at best.

8.2.4 In SEC's submission, ratepayer funds should not be spent on projects that are not primarily energy-driven. The TRC (and now TRC-plus) test is designed to calculate the incremental cost spent for incremental energy savings, and assess whether it is, overall, a good idea. If the incremental cost is $121,050 to get 1,098 cubic meters of annual savings and 385 kwh. of electricity savings, that is not a good idea.

8.2.5 We note that this is not an isolated incident. On the same list that includes 436 years and 295 years, there are also projects with paybacks of 114 years, 92 years, and 91 years. The average payback of all of the projects on the list was almost 50 years, yet most of the measures were windows, which don't last that long.

8.2.6 In our submission, the utilities should not be incenting projects that do not, on an

[78] B.T5.Union.Staff.16 Attachment 1, page 2, also found at K2.4, p. 28.
[79] One of the projects is Pipe Insulation, with a 436 year payback. Pipe insulation does not last 436 years.
[80] Tr.3:30-31.

individual basis, demonstrate cost-effective use of ratepayer funds. If the customers want to go ahead with those projects anyway, for non-energy reasons, great, but the utility should be redirecting energy efficiency money to projects that really deliver cost-effective energy efficiency.

8.2.7 What we found, after questioning utility witnesses, is that neither utility makes it a practice to ensure that custom projects they support are cost effective, on any test, whether TRC, payback, or otherwise[81]. We asked Mr. Goulden about that at the Technical Conference, and the (somewhat lengthy) exchange was instructive:

> *"MR. SHEPHERD: All right, I see. Next is tab 8, SEC 25. We asked you to confirm that each custom project would have a net positive TRC, or you wouldn't do it. And your answer was no, you don't.*
> *I'm not sure I understand why you would do a project if it didn't have a positive TRC.*
> *MR. GOULDEN: Let me perhaps give an illustrative example. We're not required to screen individual projects, and we haven't screened them. And an example of how you might have a good project that might have a negative TRC would be something like a building automation system.*
> *So as a result of discussions with the customer, the customer determines they want to install a building automation system. There are a lot of benefits associated with that building automation system. One of the most significant benefits is around the energy savings, but there is other benefits as well. You're saving time, so you're potentially saving staff time. You have potentially greater productivity in the plant as a result of building an automation system.*
> *When we do the project, we would actually identify the costs associated with the building automation system project. We don't necessarily have the ability to peel-out those pieces of the building automation system project that are energy-related. So consequently, in that case, our costing might be conservative, because we would be unable to actually identify those pieces of the building automation system project that are directly related to energy, but it is still a legitimate energy saving project.*
> *So that is an example of where it might be a negative TRC, but still, in our view, a good project.*
> *MR. SHEPHERD: So if that were the case, then, you would presumably screen that project on an overall cost-effectiveness basis, not just TRC, but TRC plus other benefits to make sure that it was at least cost-effective on an overall basis, right?*
> *MR. GOULDEN: No, we don't screen individual projects. We screen the portfolio.*
> *MR. SHEPHERD: These are big projects, right? Typically they're big projects?*

[81] K2.4, p. 36-39, Excerpt from the Technical Conference Transcript.

> *MR. GOULDEN: Yes.*
> *MR. SHEPHERD: So your example is not a really good example, because in fact you wouldn't know whether the project was cost-effective or not.*
> *Forget TRC; you just wouldn't know whether it is cost-effective.*
> *[Witness panel confers]*
> *MR. GOULDEN: We'd certainly use our judgment to determine whether it was a good project or not. So we wouldn't go ahead with the project if we didn't think it was a good project. That is why we have a relationship with our customers.*
> *MR. SHEPHERD: Why wouldn't you do -- I mean, it takes an hour to do a spreadsheet to figure out whether it is cost-effective. Presumably, the client has the customer has the data. Why wouldn't you do that for every one of these projects? They're big enough; you've only have fifty or a hundred of them.*
> *MR. GOULDEN: As I identified, you don't necessarily have the ability to peel-out the energy related costs associated with the project independently.*
> *Consequently, in terms of assessing the project, you don't necessarily have energy-only data that you can use to do screening.*
> *MR. SHEPHERD: But you said you would use your judgment to see whether there is other benefits, so that if it's negative TRC -- of course, you wouldn't even know whether it is negative TRC, right, because you never do that analysis?*
> *MR. GOULDEN: We don't on an individual project basis. I was hoping to be helpful by providing an illustrative example.*
> *MR. SHEPHERD: So then how do you use your judgment to see whether it's cost-effective on an overall basis, if in fact you don't even do the calculation of TRC? I'm missing something here.*
> *[Witness panel confers]*
> *MR. GOULDEN: We determine if the project is beneficial to the customer, including having significant energy benefits.*
> *MR. SHEPHERD: But I don't understand how you determine if it's beneficial, if you don't know -- if you can't balance the costs and the benefits.*
> *I mean, if there is any benefit, it doesn't matter how much it costs? I just -- I am missing something here.*
> *MR. GOULDEN: In the example I've given and in the situation where we have negative TRC projects, it is because we can't necessarily monetize all of the benefits aside from the energy benefits, which is what I was trying to identify."*

8.2.8 This was a theme throughout. The utilities say, with respect to individual projects, "Rely on our judgment", but when we ask how they reached their conclusions, they say they didn't have good information.

8.2.9 However, even if there may have been some logic to doing projects that are not cost-effective under the TRC test, that should no longer apply. The Board is now using the TRC-plus test, which tops up the benefits with an adder to get at benefits that can't be monetized.

8.2.10 In our submission, the utilities should no longer be permitted to ignore the cost-effectiveness of individual projects (or programs – see below) because there are nebulous "other benefits". If those other benefits are non-energy benefits, the ratepayers should not be paying money to achieve them. If those other benefits are energy benefits, they are already included in the test.

8.2.11 Ratepayers give the utilities money in their DSM budgets to, in effect, "buy" future gas savings at the best prices possible. They are not given money to buy other things, and they should not be using it for that purpose.

8.2.12 ***Programs that Fail.*** Both utilities have programs, or components of programs, that do not meet cost-effectiveness tests. Union, for example, has a low-income furnace replacement program with a TRC-plus ratio of 0.37, and a low-income multi-family with a TRC-plus ratio of 0.44[82].

8.2.13 When asked about these offerings[83], Union said that they were including those programs because the social services agencies asked for them, and in any case the low income program is "not budget constrained".

8.2.14 With respect, these are not good reasons to waste ratepayer money on offerings that are not cost-effective. The funds should be diverted to offerings that are cost-effective. If Union really is doing all of the low-income projects that exist that are cost-effective, which we doubt, then they can come back to the Board and ask for their low income budget to be reduced, so that they can spend the money more wisely.

8.2.15 We note that the Residential Behavioural Program is another that is not cost-effective. We know that other parties will raise the question of why this is being pursued in those circumstances. SEC agrees that, if it truly is not cost-effective, then absent cogent justification on other grounds (none of which is as yet on the record in this proceeding), the offering should not be approved.

8.2.16 ***Custom Projects That Are Obvious Free Riders.*** Separately in this Final Argument, SEC has argued that custom projects with very short paybacks, or are otherwise obviously free riders, should not be incented and should not be included in results.

8.2.17 We note that there is another side to this issue. Where custom projects are left in the results, and captured for shareholder incentive purposes through the overall free rider rate, they still artificially improve the overall cost-effectiveness of the portfolio. As

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[82] Ex. A/3/A, pp. 96-8.
[83] B.T8.Union. GEC.59

long as the utilities continue to follow the practice of testing cost-effectiveness only at the portfolio level, the effect is that the overall cost-effectiveness of utility DSM activities is overstated.

8.2.18 This is, of course, partially improved if the obvious free riders are excluded from the outset, as we have proposed. However, there will still be some residual impact.

8.2.19 In our view, the solution is to require the utilities to test the cost-effectiveness of every offering on a regular basis, and each custom project as well. Unless a good reason can be shown for an exception, only cost-effective offerings and projects should be included in the utilities' portfolios.

8.3 ***Incremental Cost Effectiveness***

8.3.1 The other issue of concern to SEC in this area is the fact that the utilities do not test the cost-effectiveness of incremental spending on each program, or the overall portfolio. There is a point at which incremental spending is no longer a good idea. By failing to test for this, Union and Enbridge can never know when that point has been reached.

8.3.2 We discussed this issue with Enbridge in the context of their Potential Study, which showed a big jump in cost to get a more modest jump in cubic meters[84]. In a useful and thoughtful exchange[85], Enbridge agreed that it would be useful for them and the Board to have information on the incremental cost of program and portfolio expansion.

8.3.3 SEC submits that the utilities should make a regular practice of testing incremental spending, relative to forecast incremental results, to see if it continues to be a good idea to spend more money. Further, SEC recommends that the Board direct Board staff, in the potential study currently underway, to include in that study sensitivity analyses that show incremental costing of various budget expansion or reduction strategies.

[84] See K8.1.
[85] Tr. 8:109-112.

9 AVOIDED COSTS

9.1 *General*

9.1.1 SEC is aware that other parties, notably GEC and FRPO, will be dealing with issues of avoided costs in some detail. We are relying on their submissions to provide a full discussion of the issues for the assistance of the Board. While we will not necessarily agree with all of their conclusions on avoided costs, we are confident their canvass of the issues will be thorough.

9.1.2 We do have two comments, both on the avoided cost of carbon.

9.1.3 ***The Value of Carbon is Not Zero.*** First, the utilities have proposed avoided costs that do not include an amount for the actual spending avoided due to reduced carbon emissions. Implicitly, the utilities have assumed that the amount they will have to spend on carbon over the next decades will be zero.

9.1.4 In our view this is not a reasonable assumption. It is possible, perhaps even probable, that there will be some delay in Ontario's entry into the carbon market, such that the cost of carbon may not be monetized as currently scheduled. What is not reasonable is to assume that there will be no hard cost associated with carbon emissions in Ontario during the entire expected useful lives of the measures being implemented under the Plans. That is not consistent with the available evidence. Whether the cost ends up being a carbon tax, or cap and trade, or some other system not yet invented, carbon will almost certainly be monetized in the next twenty years, more likely in the next two or three.

9.1.5 ***TRC-Plus Does Not Include All of the Reasonable Cost of Carbon.*** Second, some parties may argue that the value of carbon, even if it is monetized, is already included in the 15% adder that has been included in the TRC-plus test. In our submission, this is not a reasonable conclusion.

9.1.6 This is really about numbers, so SEC asked for the conversion of current forecast carbon prices into cents per cubic metre. This would allow us to equate it to the 15% adder.

9.1.7 What can be seen is that the 15% adder is about 3 cents per cubic metre on the TRC[86]. None of the various ways of pricing carbon contained in the evidence are less than that, and some are considerably more[87]. Therefore, unless ALL of the other externalities that are included in the 15% adder have a value of zero, and the cost of carbon in the future will be at the minimum the current evidence suggests, the cost of

[86] J1.2.
[87] See, e.g. J1.3.

carbon is not included, or not fully included, in the 15% adder.

9.1.8 In our submission, common sense says it is reasonable to assume that, even without the inclusion of carbon, the 15% adder is in the right range to estimate the value of the many externalities (other than carbon emissions) that are not otherwise included in avoided costs.

9.1.9 By implication, a forecast of the cost of carbon should be included separately in the calculations of avoided costs over the lifetimes of the measures being incented by the Plans.

9.1.10 ***A More Robust Test Justifies More Rigour in its Application.*** SEC notes that, in a separate section of this Final Argument, we urge the Board to require more rigorous cost-effectiveness testing, so that ratepayer funds are not wasted. One of the bases for those submissions is that, once you improve the avoided cost calculation, you have more freedom to be tough on qualification for programs. It is less possible to justify projects with a TRC-plus ratio under 1.0 when the TRC-plus test ensures that all material impacts are included in that calculation. That is, the range of “soft” justifications – based on unquantified benefits of the projects – is reduced.

10 ACCOUNTING: RECOVERY AND DISPOSITION

10.1 *General*

10.1.1 As filed, the utilities are proposing to collect a billion dollars from ratepayers for their DSM activities. Many issues are raised with respect to how that is accounted for, and how it is collected from customers.

10.1.2 In this Final Argument, however, SEC will deal with only two of them:

(a) Union's rate recovery from classes M1 and 01, and in particular its non-compliance with the $2.00 per month guideline, and its collection of residential program costs from commercial and industrial customers.

(b) The proposal by some parties to rate base DSM expenditures.

10.2 *Union Gas - Cost Allocation and Rate Design*

10.2.1 SEC is concerned about the cost allocation and rate design approach by Union for rates M1 and 01. While these two classes comprise primarily residential customers, they also include most small commercial and industrial customers, and about 80% of the schools in the Union franchise area. Non-residential customers are small in number in the class, but make up 24.8% of the volumes in Rate M1, and 27.2% of the volumes in Rate 01[88]. Thus, schools and other non-residential customers must be concerned about the cost of Union's residential DSM programs, whereas with Enbridge, which has a separate residential class, that is not a concern.

10.2.2 SEC has two concerns. First, it would appear that Union has failed to follow the Board's guideline of $2.00 per month maximum bill impact for residential non-participant customers. Second, the use of solely volumetric rates to recover DSM costs means, in the M1 and 01 classes, that commercial and industrial customers in those classes, including schools, are forecast to pay 130% of their share of DSM costs in 2016, rising to 273% of their share of DSM costs in 2020.

10.2.3 ***Respect for the Bill Impact Guideline.*** Union claims that, based on their assumed average residential volume of 2200 m^3 per year, their Union South customers have an impact of just under $2.00 per month by 2020, and their Union North customers have an impact of just over $2.00 per month, with a weighted average of almost exactly $2.00 by the end of the Plan[89]. SEC believes that these figures are incorrect.

10.2.4 In response to questioning from SEC, Union provided its actual figures for average

[88] B.T13.Union.GEC.7, p. 3.
[89] Ex. A/3, p. 67.

residential use[90]. In 2014, the latest year for which there is actual data, the actual average residential use was 2,583 m^3 per year, and the weather normalized average use was 2,300 m^3 per year.

10.2.5 Further, in calculating potential bill impacts Union assumed that it would not use the DSMVA, that it would achieve no more than 40% of its available shareholder incentive, and there would be no LRAM for rate M1 and 01. The latter may be reasonable, in light of the current IRM structure, but the first two assumptions are not reasonable.

10.2.6 SEC has now taken the filed information and, using the lower average use, 2,300 m^3 per year, but looking at two levels of spending: a) just the base budget, with no DSMVA and zero shareholder incentive; and b) 15% DSMVA and full shareholder incentive. Both scenarios still exclude LRAM. The results are as follows:

Union Gas Rate M1/01 Bill Impacts

(@2300 m^3 per residential customer)

	2016		2020	
	Rate M1	Rate 01	Rate M1	Rate 01
Budget	$23,194,000	$8,628,000	$28,506,000	$10,618,000
Volume Billing Units	2,921,516,000	927,922,000	2,921,516,000	927,922,000
Cents/m3 charge	0.7939	0.9298	0.9757	1.1443
Monthly @2300	$1.52	$1.78	$1.87	$2.19
Total Cost	$31,582,000	$11,181,000	$38,057,000	$13,571,000
Cents/m3 charge	1.0810	1.2050	1.3037	1.4626
Monthly @2300	$2.07	$2.31	$2.50	$2.80

Source: B.T10.Union.SEC.27 Attach. 1

10.2.7 It is submitted that, on Union's own numbers, they go above the $2.00 maximum for at least one group of residential customers, Rate 01, even if there is no DSMVA and no shareholder incentive.

10.2.8 Further, it gets much worse if the Board looks at the maximum cost to which it would be committing residential ratepayers by approving the Union Plan. Beginning immediately, and increasing over the Plan term, residential customers in both M1 and 01 will at all times be committed to spending more than $2.00 per month on Union's DSM programs.

10.2.9 In SEC's submission, this should not be accepted by the Board.

[90] J3.14.

10.2.10 It is relatively easy to calculate the maximum budget available based on the Board's guideline. If applying the volumetric approach to recovery, Rates M1 and 01 should, together, pay no more than 1.0435 cents per m^3 in total by 2020[91]. With total volume forecast of 3.85 billion m^3 , this works out to a maximum of $40.169 million allocated to those two classes. With the maximum class share of the shareholder incentive of $6.583 million[92], the total budget including Low Income allocation and 15% DSMVA is $33.586 million, and the net before DSMVA is $29.205 million. This compares to the amount of $39.170 million proposed by Union. In fact, with a $10 million reduction in budget for M1 and 01, the average bill impact is almost exactly $2.00 per month for the average residential customer[93].

10.2.11 Below, we propose a resolution of the second part of this problem, which would integrate with the first part to solve both. However, at this point our submission is that Union should be required to reduce the budgets allocated to Rates M1 and 01 (of which between 80% and 90% is residential programs) to ensure that the average monthly bill impact for residential customers does not exceed $2.00 by 2020.

10.2.12 ***Intra-Class Inequity***. SEC explored with Mr. Tetrault the (not-new) problem of having the two "residential" classes, M1 and 01, contain significant numbers of non-residential customers. Since the residential DSM budget (and share of common costs, including low income) is essentially all allocated to those classes, and a small amount of the commercial and industrial DSM budget is also allocated to those classes, the CI customers subsidize the residential programs, and the residential programs subsidize the CI programs.

10.2.13 This is not new, but in past years the cross-subsidization largely worked out as a fair trade. That is not true in the current Union Plan. The increase in spending on residential DSM, which is good for many reasons, increases the extent to which commercial and industrial customers in M1 and 01, including schools, subsidize the residential programs.

10.2.14 SEC has calculated the impact of this in the following table, drawn from Union's data provided in Exhibit A, Tab 3[94].

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[91] $24.00 per year divided by 2300 m^3 .
[92] B.T3.Union.Staff.7, Attach 1.
[93] This was discussed with Union, when the only figure we had was 2,583, rather than the weather normalized 2,300 volume average. They do not have an answer: see Tr.3:83-85.
[94] The budget component of the allocation by class is from A/3, App. E, Schedule 1. The direct allocations of budget amounts to residential and C/I are from A/3, p. 6. The percentage of residential direct allocation (compared to total direct allocations) is applied to portfolio costs and inflation to get the residential share. The C/I share is calculated by subtracting the residential share from the total budget allocation to M1/01.

Residential Component of Budgets and Collections - Union Gas				
	2016		2020	
	Amt.	%	Amt.	%
Direct Budget	$12,145		$17,845	
Mkt Trans.	$1,042			
Total Direct	$13,187	29.60%	$17,845	33.10%
Portfolio	$3,472		$1,868	
Inflation	$280		$1,712	
Total Residential	$16,939	80.52%	$21,425	90.71%
Total Allocation (Budget Component)	$21,036		$23,619	
C/I Component	$4,097	19.48%	$2,194	9.29%
Total Allocation	$42,763		$51,628	
C/I Component	$8,329		$4,796	
C/I Volumes	25.55%		25.55%	
C/I Collections	$10,926	131.19%	$13,191	275.05%
Overcollection	$2,597		$8,395	

10.2.15 What this shows is that the rate responsibility of non-residential customers is 25.55%, while their share of the costs is actually 19.48%. This is relatively close, although still a $2.6 million intra-class subsidy. C/I customers in rates M1/01 would be paying 31% more than they are getting.

10.2.16 The situation gets much worse by 2020. By that time, the C/I share of M1/01 costs drops to 9.29%, but they are still paying 25.55% of the costs. Their subsidy balloons to $8.4 million.

10.2.17 In our submission, the problem here arises solely because Union recovers DSM costs entirely through the volumetric charge. This will always result in some level of subsidy by larger volume customers to smaller. SEC believes that the results in this case show that the subsidy has become bigger than is reasonable.

10.2.18 To fix this problem, SEC proposes that all DSM costs associated with residential programs, as well as their share of all common costs, should be recovered in the fixed monthly charge. All DSM costs allocated to M1/01 for C/I programs, as well as their share of all common costs, should be recovered in the volumetric charge, excluding the first two blocks (which total 250 cubic meters per month). The effect of this approach would be that there would still be a small amount of cross-subsidization, but it would not be material.

10.2.19 One additional advantage of this approach is that it is relatively straightforward to solve the problem of meeting the $2.00 per month guideline. The fixed monthly charge for DSM cannot exceed $2.00, including all adders such as DSMVA and shareholder incentive. The budget for residential is adjusted accordingly.

10.2.20 We have seen a draft of the submissions of LPMA on M1/01 rate recovery, and we agree with and support their analysis and conclusion.

10.3 ***Rate-Basing DSM***

10.3.1 A number of parties have suggested that DSM costs should be added to rate base, thus reducing the upfront cost of that spending. This is not a viable concept, and should be rejected by the Board.

10.3.2 SEC discussed this question with Enbridge witnesses[95]. We took them to information filed that showed the very low amounts included in rates if DSM amounts are added to rate base instead of being recovered as spent[96]. They made clear, though, that all this does is defer the payment of the cost, and add cost of capital on top of it. As Mr. Lister said "They pay it over a long period of time, and subject to what cost of capital I don't know, and a whole bunch of other accounting issues".

10.3.3 Rate basing DSM costs doesn't change the upfront cost of the DSM. What it changes is the method of payment. In the current system, we pay as we go, with the cash in our wallets. In the rate-basing approach, we put it on the credit card and pay it, with a high carrying cost (WACC is over 6%, plus tax, making the overall rate close to 8%), over time.

10.3.4 This is not a good deal.

[95] Tr.6:48-50.
[96] Jt1.33. Also in K5.5, p. 99-107.

11 GAS/ELECTRIC CO-ORDINATION

11.1 *General*

11.1.1 One of the key priorities expressed by the Board in the Framework is increased co-ordination and integration between gas and electric DSM programs. This is facing significant challenges, and while steps are being taken, it is agonizingly slow.

11.2 *Challenges*

11.2.1 ***Bifurcated Jurisdiction.*** A significant part of the problem is that the Board has jurisdiction over gas DSM programs, but IESO has jurisdiction over the electricity CDM programs. It was a theme throughout the Applications and the evidence on this point that the gas utilities can only do so much, but if the LDCs don't want to work jointly with the gas utilities, there is nothing the gas utilities (or the Board) can do to force that.

11.2.2 In fact, if the Board does try to push the gas utilities to work more with the electrics, it could put them at a disadvantage[97]:

> *"MR. SHEPHERD: And the reason why I'm asking this is because, in the simplest terms, this Board can simply say to you, for a program that clearly should be offered jointly like home energy conservation, "We're not going to let you offer that unless it is joint with the LDCs."*
> *They could just say that to you, right? And then you'd have no choice. You would have to have a deal with the LDCs, right?*
> *MR. LISTER: I suppose that could be an alternative that the Board considers.*
> *MR. SHEPHERD: But the problem with that would be that then basically you'd have to do whatever programs the LDCs or IESO wanted. You wouldn't have any say in the matter. You'd be -- you would have no negotiating position.*
> *MR. LISTER: By default, we'd be -- I'll say at the mercy of that process."*

11.2.3 What the gas utilities are doing, to a greater or lesser extent, is the slow process of working collaboratively on IESO committees and in bilateral discussions with utilities. This is not going to make anything happen quickly, but it is, in our submission, the only option available to them.

11.2.4 In some areas, it appears that this collaboration is already bearing fruit. Enbridge points out, for example, that in low income projects the gas utility and the electricity distributor often do their presentations together[98]. They are offering different

[97] Tr.8:99-100.

programs, but for the social housing agency or other customer, it is in some respects a joint activity.

11.2.5 All of this gentle persuasion and discussion may be frustrating, but in our submission the current jurisdictional structure makes it inevitable. The utilities should be encouraged to continue to push these goals.

11.2.6 ***Competing with Ourselves.*** The other way in which the gas utilities are seeking to respond to the activities of the LDCs is by increasing incentives. They do this to get the attention of the customers, who otherwise would be more attracted to the much richer incentives available for electricity conservation measures.

11.2.7 Enbridge described this as follows:

> *"MR. SHEPHERD: And did I hear you agree with me that on -- in terms of how many dollars you can give to the customer, for the most part you can't actually compete with the electrics?*
> *MR. LISTER: I would say that's been one of our observations, and one of the things that guided us in the -- in this plan, and I think if you go through Exhibit B2.1, through all of the program and offer descriptions, we cite that often as a barrier to many of our programs.*
> *We'll show up at a customer's door and say, We've got some great ideas, we can help you financially and technically, are you interested, and once they see the economics they'd rather pursue the electric alternative in many cases, because that incentive money is -- it's bigger, it's more impactful, whatever the situation might be."*

11.2.8 Of course, often the gas utilities can get customer traction anyway, either due to their ongoing relationships with customers, or the expertise they bring to the table.

11.2.9 But the other thing they are doing is offering bigger cheques, and SEC believes that this is generally not in the interests of the ratepayers.

11.2.10 The problem here is that the money being spent by the LDCs is the ratepayers' money, and the money being spent by the gas utilities is the ratepayers' money. We are bidding against ourselves if we allow both conservation providers to compete to get the attention of potential program participants.

[98] Tr.7:82-3.

11.2.11 If you hired two real estate agents to find a house or other building that suits your needs, you would make absolutely sure that they didn't end up bidding against each other for the same building. That is only going to waste your money. The same thing is true here. The gas utilities should not be increasing their incentives to compete with the electricity distributors. That is just wasting our money.

11.2.12 SEC therefore believes that the Board should direct both Union and Enbridge to review all of their proposed program incentives and other benefits, and determine which, if any, are higher than they would need to be, absent competition from electricity distributors. Where that is the case, they should be reduced to a more reasonable level, and the gas utilities should discuss with the LDCs and IESO the need to co-ordinate their offerings so that the electricity distributors are also not spending more than necessary.

11.3 ***Conclusions and Recommendations***

11.3.1 Many of the programs and offerings proposed in the Plans would be better – sometimes significantly better – if they were offered jointly with the electricity distributors. Examples include the Residential Behavoural offering, Home Rating, Home Reno Rebate, and Home Energy Conservation, to name just a few. When we talked with the utility witnesses, they didn't hesitate in their support for making many of these programs joint.

11.3.2 They can't do it alone, and this Board cannot force the issue within its specific jurisdiction. SEC believes that the patience and tenacity that Union and Enbridge have expressed as their goals in this regard are the best that can be done. The Board should not expect any meaningful steps in this direction in the near term.

12 INFRASTRUCTURE PLANNING

12.1 *Analysis*

12.1.1 In listening to the evidence in this proceeding, SEC got no sense that either utility feels integration of DSM with infrastructure planning is a matter of any urgency. This stands to reason. Central to the role of the gas distributor is putting pipe in the ground. Their whole profitability structure is built on that edifice. Active planning to avoid laying pipe is directly contrary to their interests.

12.1.2 SEC therefore believes that, if the Board wants this to be done, it must take a more active role. To that end, SEC recommends that the Board take two steps:

(a) Initiate a consultation between the gas utilities and their stakeholders, including external experts hired by the Board, to establish a framework for the integration of DSM and infrastructure planning.

(b) Upon completion of the consultation, and delivery of the Board's framework and guidelines, set a hard deadline for receipt of comprehensive DSM/infrastructure plans from each of the utilities.

13 OTHER MATTERS

13.1 *Costs*

13.1.1 The School Energy Coalition hereby requests that the Board order payment of our reasonably incurred costs in connection with our participation in this proceeding. It is submitted that the School Energy Coalition has participated responsibly in all aspects of the process, in a manner designed to assist the Board as efficiently as possible

All of which is respectfully submitted.

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Jay Shepherd
Counsel for the School Energy Coalition