

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 a generic hearing on the
Expansion of Natural Gas Service to Ontario Communities.

Proposed Issues List

Submissions of the

Energy Probe Research Foundation

February 26, 2016

**Schedule A
To Procedural Order No. 1
EB-2016-0004
Draft Issues List
February 10, 2016**

Context for Comments

Energy Probe is a non-profit environmental and consumer organization which promotes economic efficiency in the use of resources. Energy Probe is representing its residential customer supporters in Ontario, of which we have some number of thousands, and also representing a broader public interest concern with respect to the overall financial health and operational integrity of our utilities. Energy Probe will address issues which the Foundation believes to be in the residential ratepayer interest.

In preparing its Comments Energy Probe notes it has not retained Legal Counsel. Its comments on Regulatory aspects are based on a plain reading of the Legislation, Guidelines and its understanding of the Board's Practice.

**Draft Issues List
February 10, 2016**

1. Does the OEB have the legal authority to establish a framework whereby the customers of one utility subsidize the expansion undertaken by another distributor into communities that do not have natural gas service?

Comments:

In our view, there is no case – either on ratemaking principles or through OEB legislation – that would allow ratepayers of one utility to subsidize the rates of another.

Rates are set under Section 36 of the OEB Act and must in our view meet, inter alia, the requirement that they are just and reasonable and reflect the costs to the utility of providing gas distribution service to its customers.

We aren't aware of any case in Ontario where the customers of one gas utility subsidize the customers of another, while there are a number of cases where distributors in Ontario charge unsubsidized rates to other distributors operating in the province, such as:

- Rates charged to Enbridge, TCPL, Gaz Metro and others that use Union's Dawn to Parkway System under M12 rates,

- **Rates charged to NRG, Kingston and Kitchener Utilities that use transmission systems of Union and Enbridge.**

Therefore for these reasons we submit this issue, as worded, is inappropriate and should be dropped from further consideration.

2. Based on a premise that the OEB has the legal authority described in Issue #1, what are the merits of this approach? How should these contributions be treated for ratemaking purposes?

Comments:

Energy Probe will leave it to legal counsel to address the presumption regarding legal authority.

In our view, the only subsidies that the Board has in the past found reasonable are detailed in the EBO188 Guidelines and are related only to customers of one utility. Under those guidelines, the level of subsidy from current to future customers is limited in scope and scale and does not concern cross subsidies between customers of different utilities.

Contributions from taxpayers and municipalities are outside of this basic consideration.

3. Should the OEB consider exemptions or changes to the EBO 188 guidelines for rural and remote community expansion projects?

- Should the OEB consider projects that have a portfolio profitability index (PI) less than 1.0 and individual projects within a portfolio that have a PI lower than 0.8?

Comments:

E.B.O. 188 Appendix B describes the Rolling Portfolio

1.2 Rolling Project Portfolio

Each of the utilities will maintain a rolling 12 month distribution expansion portfolio (the "Rolling Project Portfolio") updated monthly, as an ongoing management tool for estimation of the future impacts of capital expenditures associated with distribution system expansion. The Rolling Project Portfolio will exclude those customers requiring only a service lateral from an existing main.

The utilities will calculate monthly the cumulative result of project-specific DCF analyses from the past twelve months for the Rolling Project Portfolio. It will include all future customer attachments, revenues and costs on the basis of the life cycle of each of the projects making up the Portfolio.

The Rolling Project Portfolio assumes that the gas utilities currently have a forward-looking portfolio of economic expansion projects. Union has indicated in its recent Application that this may not be the case. Without such a base of economic expansion projects to rural and remote communities, E.B.O. 188 criteria cannot be accommodated without undue subsidy.

It is suggested that Union and Enbridge should project their system expansion portfolios over a longer period of 5 years, coincident with the time-frame of any community expansion program

- What costs should be included in the economic assessment for providing natural gas service to communities and how are they to be determined and calculated.
- What, if any, amendments to the EBO 188 Guidelines would be required as a result of the inclusion of any costs identified above?

Comments:

The Economic Tests for E.B.O. 188 Distribution/Community expansion derive from those set out for system expansion under E.B.O. 134. The two sets of Guidelines each require a Discounted Cash Flow (DCF) methodology that is used to generate a Profitability Index.

The similarities and differences are shown in the Table below:

Comparison of E.B.O. 134 and E.B.O. 188 Guidelines

Guidelines	E.B.O. 134 System Expansion	E.B.O. 188 System/Community Expansion
Applicability	Transmission Pipelines (Compressors exempt)	Transmission/distribution laterals and services
Date Issued	June 1, 1987 Confirmed in Filing Guidelines EB-2013-0092	January 30, 1998
Economic Tests	DCF Cash Flow Analysis Horizon 40 years Discount Rate- Utilities' incremental after-tax cost of capital	DCF Cash Flow Analysis Customer Attachment 10 years Horizon 40 years Discount Rate- Utilities' incremental after-tax cost of capital
Profitability Index Targets	Phase 1 ≥ 1.0 Phase 2 Cost/Benefit to Utility Customers (in franchise) Phase 3 Other Cost/Benefit considerations	0.8-1.0 If SE portfolio ≤ 1.1

A plain reading of the Initial E.B.O. 134 Decision shows that the main considerations in the Bosard's Report of 1987, included Community Expansion.

However the practice has been to separate Transmission and Distribution expansion.

Extract from E.B.O. 134 Decision re Methodology/Approach:

- 6.72 The Board finds that Union's three-stage test has considerable merit. The Board requires each utility to develop a three-stage process as outlined below to aid the Board in its determination of the public interest.**
- 6.73 The first stage is a test based on a DCF analysis.**
- 6.74 The second stage should be designed to quantify other public interest factors not considered at stage one. All quantifiable other public interest information as to costs and benefits should be provided at this stage.**
- 6.75 The third stage should take into account all other relevant public interest factors plus the results from stage one and stage two.**

Accordingly, the Economic Feasibility tests for both pipelines (as detailed in EBO 134) and distribution and community expansions (as detailed in EBO 188) are similar and use the same generic methodology. It is our view, then, that any review of the system/community expansion regulations should also encompass changes (if there are any) to the basic DCF methodology for both. This is critical because any community expansion program may also result in upgrading upstream infrastructure – and the resulting tests that such an upgrade with kick start.

We note that one major difference between EBO 134 and EBO 188 is the inclusion in E.B.O. 134 of Stage 2 and Stage 3 Cost/Benefit analyses. As noted above, these additional stages aim to address certain public interest considerations – including fuel savings to new customers (Stage 2) and economic development (Stage 3) – that weren't covered by a simple DCF test.

A number of recent expansion proposals for the Dawn-Parkway system that were primarily for ex-franchise shippers, such as Enbridge and Gaz Metro, have failed the E.B.O. 134 Stage 1 Economic Test, but have relied upon Stage 3 Benefit/Cost analysis to justify their approval.

In the original EBO 134 Decision, public interest considerations were addressed at paragraph 5.3 and in the Board's subsequent comments.

- What would be the criteria for the projects/communities that would be eligible for such exemptions? What, if any, other public interest factors should be included as part of this criteria? How are they to be determined?

Comments and EP suggestion:

We suggest the following:

What would be the criteria for the projects/communities that would be eligible for such exemptions? What, if any, other public interest factors should be included as part of this criteria? What, if any, social justice factors be included as part of this criteria? Should social injustice factors, such as the forced expropriation of private property, be considered when an otherwise uneconomic project is proposed? How are the non-economic factors – public interest, social justice and social injustice factors – to be determined?

4. Should the OEB allow existing natural gas distributors to establish surcharges from customers of new communities to improve the feasibility of potential community expansion projects? If so, what approaches are appropriate and over what period of time?

Comments:

Contributions in Aid of Construction have been an established part of gas system expansion for some time.

The new twist in regards to the Directive that will push the gas distributors to service marginal (cost to serve) communities is that the amount of contribution required for many such communities is

- Too large, and
- Not possible for customers to provide upfront.

Union wants to mitigate these barriers by extending the new customer CAAC period up to 10 years (aided by a forecast of low future gas commodity prices) and is seeking an additional contribution of avoided municipal tax from the project. However, this approach doesn't consider the impact of provincial loans or grants that will allow certain projects to proceed on the basis of economic, social or other considerations – which are the domain of the province, not existing utility ratepayers. The real need is for the province to make natural gas a key factor in its economic and social programs AND critically, put in the money to make this happen. Putting that onus on existing ratepayers goes against the nature of how the sector has traditionally been regulated in Ontario.

6. Should the OEB allow for the recovery of the revenue requirement associated with community expansion costs in rates that are outside the OEB approved incentive ratemaking framework prior to the end of any incentive regulation plan term once the assets are used and useful?

Comments:

Separating the Community Expansion projects and Revenue Requirement is, in our view, contrary to establishing just and reasonable rates (including by IRM) and raises the thorny issue of determining how the costs will be recovered given the timing differences between the amounts charged in rates and revenues from Community Expansion customers

7. Should the OEB consider imposing conditions or making other changes to Municipal Franchise Agreements and Certificates of Public Convenience and Necessity to reduce barriers to natural gas expansion?

No comments pending further consideration of this issue

8. What types of processes could be implemented to facilitate the introduction of new entrants to provide service to communities that do not have access to natural gas. What are the merits of these processes and what are the existing barriers to implementation? (e.g. Issuance of Request for Proposals to enter into franchise agreements)

Comments:

One outcome of this hearing should be creation of a level playing field to allow existing and new entrants the opportunity to provide natural gas service – or competing services – at the lowest economic cost in order to reduce subsidies, loans and grants in the sector. If existing barriers prevent this, then the province should be advised of this by the Board.

Based on the above Comments Energy Probe suggests the Issues List be modified as follows:

~~1. Does the OEB have the legal authority to establish a framework whereby the customers of one utility subsidize the expansion undertaken by another distributor into communities that do not have natural gas service?~~

~~2. Based on a premise that the OEB has the legal authority described in Issue #1, what are the merits of this approach? How should these contributions be treated for ratemaking purposes?~~

3. Should the OEB consider exemptions or changes to the EBO 188 Guidelines for rural and remote community expansion projects?

o Should the OEB consider projects that have a portfolio profitability index (PI) less than 1.0 and individual projects within a portfolio that has a long term rolling PI>1.0 and that have a PI lower than 0.8?

o What costs should be included in the economic assessment for both System Expansion (E.B.O. 134 Pipelines) and providing natural gas distribution service to communities (E.B.O. 188) and the methodology for the Economic tests.

o What, if any, amendments to the EBO 134 and EBO 188 Guidelines would be required as a result of the methodology identified above?

o What would be the criteria for the projects/communities that would be eligible for such exemptions from the EBO 188 Guidelines? *What, if any, social justice factors be included as part of this criteria? Should social injustice factors, such as the forced expropriation of private property, be considered when an otherwise uneconomic project is proposed? How are the non-economic factors -- public interest, social justice and social injustice factors -- to be determined?*

4. Should the OEB allow ~~existing~~ natural gas distributors to establish surcharges from customers of new communities to improve the feasibility of potential community expansion projects? If so, what approaches are appropriate and over what period of time?

5. Are there other ratemaking or rate recovery approaches that the OEB should consider?

6. Should the OEB allow for the recovery of the revenue requirement associated with community expansion costs in rates that are outside the OEB approved incentive ratemaking framework prior to the end of any incentive regulation plan term once the assets are used and useful? If so, how would this be done while ensuring just and reasonable rates?

7. Should the OEB consider imposing conditions or making other changes to Municipal Franchise Agreements and Certificates of Public Convenience and Necessity to reduce barriers to natural gas expansion?

8. What types of processes could be implemented to facilitate the introduction of new entrants to provide service to communities that do not have access to natural gas. What are the merits of these processes and what are the existing barriers to implementation? ~~(e.g. Issuance of Request for Proposals to enter into franchise agreements)~~

NEW

9. Following the generic hearing, the Board should provide a report to the Minister with its recommendations regarding provision of gas service to un-served Ontario Communities.