EB-2016-0004

Ontario Energy Board

IN THE MATTER OF
GENERIC PROCEEDING ON NATURAL GAS
EXPANSION IN COMMUNITIES
THAT ARE NOT SERVED

VULNERABLE ENERGY CONSUMERS COALITION
("VECC")
CROSS-EXAMINATION COMPENDIUM

SOUTH BRUCE

May 9, 2016

TAB 1

After the Municipalities held meetings with all 6 proponents and after obtaining further information from proponents in a second phase of the RFI process, 4 finalist proponents were evaluated by the Municipalities.

In the end, the Municipalities selected EPCOR as their preferred proponent. The three Municipalities each approved and signed a Franchise Agreement with EPCOR on February 22, 2016.

Benefits of the Competitive Solicitation Process

While the process followed by the Municipalities was time consuming and costly, it had a number of important benefits which are summarized below.

1) Providing an opportunity for alternative approaches

Initially the Municipalities were constrained to information being provided by the only gas distributor in the region. The RFI process allowed other interested parties an opportunity to provide alternative views on meeting the region's natural gas needs. The participants in the process brought different experiences and approaches to the resolution of problems and did so within the framework of a competitive process.

2) Understanding of the energy market in the region

Through the submissions of the participants the Municipalities improved their understanding of the size and composition of the potential market for natural gas in Southern Bruce. Related to this came more accurate estimates of the possibilities for savings in energy costs by various customer classes.

Equally important was the additional information provided on impediments to conversion to natural gas that could undermine project economics. Recommendations were also given on measures to overcome them.

3) System Design and Cost

The respondents to the RFI provided alternative approaches to system design and staging and the links between these elements and market development. In this competitive environment they also provided alternative views on capital cost estimates which resulted in a significant reduction from the initial estimates. All of these, of course, are critical to project viability.

4) Customer Rates Estimates

The estimated rates differed significantly between Union and the other participants in the process. In the Union study referred to above the utility was constrained to charge existing rates to new customers and to make up for the resulting non-economic nature of the project via a CIAC to be paid by the Municipalities. The other submitters viewed the project as stand-alone and determined the rates required to make it economically viable. This provided a better understanding of the scope for allocating expansion costs to those benefitting directly from the project via rates higher than current Union rates in the broader area.

5) Role of Subsidies

The information described above provided the Municipalities with a better understanding of the role that subsidies might play, whether originating with government programs or other consumers, and their potential magnitude. Different views were expressed on how any such subsidies would be used.

6) Ownership Options

Whereas the initial proposals for expansion were limited to two municipal ownership options, either none or all, the RFI process resulted in a range of ownership possibilities, including the gradual assumption of ownership over time. With the RFI process, the Municipalities could also individually decide on the preferred level of ownership individually after consideration of likely rewards and risks.

7) Regulatory Restrictions

The RFI process clarified the nature of the regulatory restrictions that impeded the expansion of natural gas markets. The major impediments in this regard included the combination of using current rates and a profitability index of 1.0 to

TAB 2

South Bruce Interrogatory Responses

EXHIBIT S13

Exhibit R13.South Bruce. Board Staff.2

Reference: Expansion of Natural Gas Distribution in Southern Bruce County, October 6, 2014, Appendix C. Pages 34-35

Interrogatory:

The report states that AMEC Environment and Infrastructure and Energy Fundamentals Group reviewed the Union Gas Limited (Union) Proposal to provide gas distribution services to Kincardine and surrounding areas. AMEC concluded that Union's proposed project may not be justified or practical. They recommended consideration of an alternative that would involve replacing the transmission part of the proposed project with the infrastructure necessary to allow the delivery of Compressed Natural Gas (CNG) to distribution facilities. AMEC believed that such an option would save about $60 million in capital spending and allow the project to proceed in stages.

a) Did Southern Bruce consider the option of sourcing Compressed or Liquefied Natural Gas in place of building a transmission line? Please provide a detailed response including any reasons for not considering such an option.

b) Did Southern Bruce try to verify AMEC's claim of saving $60 million if a CNG option was pursued?

Response:

a) This was considered at page 35 of the business case analysis attached as Appendix “C” to the municipalities report. It concludes that while AMEC/EFG felt the alternative was technically feasible, they lacked the cost information to justify a more definitive conclusion regarding the commercial viability of this alternative. The AMEC report provided no details on the economics of the CNG option. The estimated saving of $60 million was obtained by simply removing AMEC’s estimate of the transmission component of UGL’s capital expenditure estimate.

b) As part of the competitive RFI process, the municipalities tested the market for innovative solutions to meet their local needs.

The competitive RFI process did not limit technological innovation. As described in the evidence, Northern Cross proposed a novel approach that proposed to utilize gas storage.

South Bruce Interrogatory Responses

EXHIBIT S13

Exhibit R13.South Bruce.CCC.2

Reference: the Municipalities Report/pp. 4-5

Interrogatory:

Preamble: Union estimated that the capital expenditures for the project would be close to $97 million and that the resultant required CIAC paid by the Municipalities would be just under $86 million (based on forecast 2012 costs).

[Re: Northern Cross Proposal] The development of the new natural gas delivery system would consist of three phases with total capital expenditures amounting to $70.2 million, substantially less than the Union proposal.

What is EPCOR's total estimate for the capital expenditures for it to provide natural gas distribution to the Municipalities?

Response:

The proposals received by the municipalities in response to the RFI process that was conducted are strictly confidential and commercially sensitive information. In addition, EPCOR's estimates are not directly relevant to the issues this Board panel is considering in this EB-2016-0004. On EPCOR's web site information provided on the project states that capital expenditures will be between $100 m and $120 m.

TAB 3

South Bruce Interrogatory Responses

EXHIBIT S13

Exhibit R13.South Bruce. Board Staff.8

Reference: Exhibit 1, Pages 34-35

Interrogatory:

A theme that is central to these developments and the Board's Issues List is a re-examination of the system expansion methodology currently used by the OEB-regulated natural gas distributors and, more fundamentally, an examination of the most efficient and effective means of extending natural gas service to unserved communities, particularly those that do not meet the current EBO 188 economic feasibility criteria.

The Issues List in this proceeding does not actually presuppose that any changes to EBO 188 will be made. Issue 4 states: "Should the OEB consider exemptions or changes to the EBO 188 guidelines for rural, remote and First Nation community expansion projects?"

Elenchus' Report examines "the most efficient and effective means of extending natural gas service to unserved communities, particularly those that do not meet the current EBO 188 economic feasibility criteria". Did Elenchus take it as a given that changes would be made to the existing framework? In other words, is the Elenchus' Report focussed on "how" the Board could adjust its processes to allow for more gas expansion, not "if" the Board should do so?

Response:

The Elenchus report addresses mechanisms that have been used to achieve the objective of expanding the availability of utility services (natural gas distribution, electricity transmission and telecommunications services) to make projects economic and/or utility services available at affordable prices. It demonstrates that a variety of approaches have been used, including implicit and explicit cross-subsidies, as well as government subsidies of service providers and/or customers. While the Elenchus report suggests that a wide range of options are available to address the issues being examined in this proceeding, it does not make recommendations as to whether or how the current EBO 188 economic feasibility criteria might be revised.

Mr. Todd notes that the Southern Bruce approach to system expansion by EPCOR to serve the Southern Bruce region would neither require nor preclude changes to the EBO 188 criteria.

TAB 4

South Bruce Interrogatory Responses

EXHIBIT S13

Exhibit R13.South Bruce.BOMA.83

Reference: The approach and competitive solicitation process undertaken by the Municipalities to facilitate the expansion of Natural Gas Service to Southern Bruce County, March 21, 2016

Interrogatory:

Did the franchise agreements signed by the three municipalities with EPCOR depart in any way from the existing Model Franchise Agreement? If so, how? Please make copies of these franchise agreements available. When will the municipalities or EPCOR submit the franchise agreements to the Board for approval?

Response:

Yes. The franchise agreements were filed with the OEB for approval pursuant to Section 8 of the *Municipal Franchises Act*. These agreements will be the subject of OEB review pursuant to this separate application.

The form and content of these agreements are not relevant to the issues this Board panel is considering in this EB-2016-0004.

March 24, 2016

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, 27th Floor
Toronto, Ontario M4P 1E4

Dear Ms. Walli:

Re: The Municipality of Arran-Elderslie

Attached is an Application by EPCOR Southern Bruce Gas Inc. for Orders of the Board with respect to a Franchise Agreement with and Certificate of Public Convenience regarding the Municipality of Arran-Elderslie.

The proposed Franchise Agreement is in the form of the 2000 Model Franchise Agreement with amendments agreed to between EPCOR and the Municipality.

Please do not hesitate to contact me should you have any questions. I look forward to receipt of your instructions.

Yours truly,

[*Original signed by Bruce Brandell*]

Bruce Brandell
Director, Commercial Services
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Encls.

15. EPCOR applied to the Council of Arran-Elderslie for a franchise permitting EPCOR to construct and operate works for the distribution and transmission of natural gas in the Municipality. On February 18, 2016, the Council of Arran-Elderslie gave approval to the form of a Franchise Agreement in favour of EPCOR and authorized EPCOR to apply to the Ontario Energy Board (the "**Board**") for approval of the terms and conditions upon which and the period for which the Franchise Agreement is proposed to be granted.

16. Arran-Elderslie and EPCOR negotiated a form of Franchise Agreement in favour of EPCOR, which is for a term of 20 years and which differs from the 2000 Model Franchise Agreement as follows:

   (a) Section 4 of Part II of the Franchise Agreement contains termination provisions. If EPCOR fails to meet certain milestone dates at various points throughout the regulatory applications and construction of the gas system, the Municipality has termination rights under the Franchise Agreement. If EPCOR is able to meet the milestone dates contained in Section 4 of Part II of the Franchise Agreement, the rights granted under the Franchise Agreement shall be for a 20 year term. The rationale for the additional termination provisions is to ensure that EPCOR is actively pursuing the regulatory applications for the gas system, the construction of the gas system and the operation of the gas system in a timely manner.

   (b) Section 5 of Part III of the Franchise Agreement provides for the payment of an annual fee by EPCOR to the Municipality following the commencement of operation of the gas system. The rationale for the annual fee is to allow the Municipality to earn revenue from the granting of the franchise permitting EPCOR to construct and operate works for the distribution and transmission of natural gas in the Municipality.

   (c) Section 6 of Part III of the Franchise Agreement provides for a rebate of the Municipality's portion of any property or similar taxes payable by EPCOR pursuant to the *Ontario Assessment Act* for the first ten years of operation of the gas system. The rationale for this provision is to allow EPCOR to offer a lower tariff, thereby encouraging customer conversion. This tax rebate also demonstrates the Municipality's commitment to bringing natural gas service to the area by sharing the financial cost of doing so.

   (d) Section 20 of Part IV provides for the assignment of the Franchise Agreement to a wholly or majority owned subsidiary of EPCOR. This provision was introduced to allow EPCOR Utilities Inc. to assign the Franchise Agreement to a subsidiary to carry out the construction and operation of the gas system in the Municipality.

17. On January 30, 1998, an order was made under the *Municipal Act*, R.S.O. 1990, c. M-45, effective January 1, 1999, to amalgamate the communities of the Township of Arran, the Town of Chesley, the Township of Elderslie, the Village of Paisley and the Village of Tara to form the Municipality of Arran-Elderslie (the "**Amalgamation**").

18. Through what appears to be a combination of EBLO 259 (April 30, 1997) and EBA 775 (June 4, 1997), Union has approved franchise agreements and certificates of public convenience and necessity with the pre-amalgamation Township of Arran and the Village of Tara.

4.2 Municipal Contributions: Incremental Tax Equivalent

Description

Union proposes the introduction of a municipal contribution mechanism, known as the Incremental Tax Equivalent ("ITE"), to provide municipalities with a mechanism to contribute toward project feasibility. The ITE value will be based on the estimated value of incremental property taxes collected from Union as a result of the project for a period of time that matches the term of the TES. Implementation of this mechanism would require an agreement with the municipality prior to commencement of construction.

This mechanism provides a means of satisfying the principle that each of the beneficiaries of expansion to rural or remote communities should make a contribution towards the financial viability of the project. Municipalities are one of the beneficiaries as they would see the elimination of an economic development barrier, would receive incremental property taxes from the projects that would not correspond to increases in necessary municipal service costs, and in many cases, would benefit from reduced energy costs for municipally-owned facilities.

As noted in Section 4.6, Union will capture the ITE revenues from Expansion Community municipalities in a deferral account to be disposed of annually to ratepayers.

South Bruce Interrogatory Responses

EXHIBIT S13

Exhibit R13.South Bruce.SEC.8

Reference: EB-2016-0137/138/139, Franchise Agreement, section 5

Interrogatory:

EPCOR has filed applications for approval of its Franchise Agreements with the Municipalities of Arran-Elderslie, Kinkarden (sic) and Huron-Kinloss. In each of those Franchise Agreements, EPCOR has agreed to pay each municipality an annual fee equivalent to 1% of the gross revenue derived by it for natural gas supplied for consumption within the municipality net of the commodity costs of supply. What role did the EPCOR's willingness to pay the annual fee have in their selection as the natural gas proponent for the South Bruce municipalities? Please describe the history and development of the annual fee.

Response:

EPCOR's proposed annual fee was only one of many factors considered by the Municipalities. The Municipalities understand that annual fees paid by gas utilities to municipalities are common practice in Western Canada. In the Ontario context, annual fees will help offset, over time, the municipal property tax rebate that has been requested by EPCOR to help support the economic viability of the gas expansion. The EPCOR franchise agreements were filed with the OEB for approval pursuant to Section 8 of the *Municipal Franchises Act*. These agreements will be the subject of OEB review pursuant to this separate application. The existence and rationale for any annual fees are not relevant to the issues this Board panel is considering in this EB-2016-0004.

TAB 5

South Bruce Interrogatory Responses

EXHIBIT S13

Exhibit R13.South Bruce.Union.2

Reference: Exhibit 1, Page 76 & 77

Interrogatory:

Preamble:

At p.8 of the Report prepared by the Municipality of Kincardine, the Municipality of Arran-Elderslie, the Township of Huron-Kinloss & Henley International Inc. (dated March 21, 2016) it references that the RFI obtained included information from interested parties about their direct experience including "distribution rate design".

Question:

a) Please provide a summary of the different rate design proposals that were included in the RFIs received by South Bruce.

Response:

The municipalities strongly object to third parties, including potentially unsuccessful proponents, attempting to misuse the Board's discovery process in an attempt to obtain access to information from competitive bids that were submitted in response to a confidential RFI process. In addition, the different rate design proposals received by the municipalities are not directly relevant to the issues this Board panel is considering in this EB-2016-0004.