

June 20, 2016

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Ontario Energy Board
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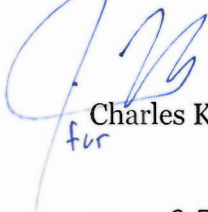
Attention: Ms. Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: EB-2016-0004 - Union Gas Limited - Natural Gas Expansion Generic Proceeding – Submissions of Union Gas Limited

We are counsel to Union Gas Limited (“Union”) in the above-referenced proceeding. Further to Procedural Order No. 3 from the Board, dated May 30, 2016, we are pleased to provide Union’s Submissions.

Yours truly,



Charles Keizer
fur

cc: C. Ripley, Union Gas
All Intervenors (EB-2016-0004)

ONTARIO ENERGY BOARD

IN THE MATTER OF an application under the Ontario Energy Board’s own motion to consider potential alternative approaches to recover costs of expanding natural gas service to communities that are not currently served.

SUBMISSIONS OF UNION GAS LIMITED

June 20, 2016

These are the submissions of Union Gas Limited (“Union”) in this matter.

A. INTRODUCTION

1. To reaffirm the Ontario government’s commitment under the Long-Term Energy Plan (“LTEP”)¹ to work with natural gas distributors and municipalities to expand natural gas infrastructure to serve more communities in rural and northern Ontario, the Minister of Energy wrote to the Ontario Energy Board (the “Board”) to encourage the Board to examine opportunities to facilitate that access. In response, by way of letter dated February 18, 2015, the Board invited parties with the appropriate financial and technical expertise to propose one or more plans for natural gas expansion. The Board further noted that it would consider requests for regulatory flexibility or appropriate exemptions in the context of an application made for approvals pertaining to expansion portfolios and specific projects.
2. In response to the Board’s letter, Union filed an application with the Board on July 23, 2015 seeking approval to provide natural gas service to certain communities that are not currently being served (EB-2015-0179).

¹ Ministry of Energy, *Achieving Balance – Ontario’s Long-Term Energy Plan* (December 2, 2013).

3. In its application, Union indicated that under its proposal it could complete approximately 29 projects to provide natural gas service to 18,000 homes and businesses in 33 communities at an estimated cost of \$135 million. Union also sought approval for rate recovery in respect of four specific projects and leave to construct approval for three of the four projects.
4. In a letter dated January 20, 2016, the Board informed all parties that it intended to proceed with a generic hearing on its own motion as the issues raised by the parties in Union's application were common to all gas distributors and new entrants seeking to provide gas distribution services to communities without access. The Board also noted in that letter that Union's application (EB-2015-0179) would be put on hold until the completion of the generic hearing and that the evidence filed in EB-2015-0179 would form part of the record in the generic proceeding.
5. As a backdrop to these developments, there has been a steady and ongoing flow of requests for natural gas distribution service from Ontario communities that remain unserved. For example, based on inquiries for services tracked by Union in the period May to December 2015, Union had approximately 1,850 inquiries of which 1,730 were not feasible because the required aid-to-construct exceeded what potential customers were willing to pay (Transcript Vol. 4, p. 167).
6. Union also encountered similar requests from municipal officials and organizations, like the Ontario Federation of Agriculture (Transcript Vol. 4, p. 167). This was reinforced clearly and directly in the current proceeding (EB-2016-0004) by the presentations from the municipal representatives of Norfolk County, Sioux Lookout, East Ferris, Perth East and Edwardsburgh-Cardinal (Transcript, Pre-hearing Conference, April 26, 2016).
7. The combined implication of the LTEP, the letters from both the Minister and the Board, as well as the numerous requests from potential customers, is that the issue before the Board in this generic proceeding is not whether regulatory changes *should* be implemented to facilitate the expansion of natural gas distribution services, but rather *how* those changes are to be implemented. Consequently, the question for the Board in this proceeding is *to what extent the current requirements established in EBO 188 are to*

be amended or applied, either working within existing parameters while permitting some internal utility cross-subsidization or ignoring the established mechanism to implement a global subsidy.

8. Three aspects that are key to the Board's considerations are:
- (i) the mechanism by which a subsidy is to be provided, since little of the expansion of distribution services contemplated in this proceeding will be possible without some form of cross-subsidization;
 - (ii) the best interests of the ratepayer, with appropriate balance between new and existing customers, which is at the heart of the above issue; and
 - (iii) recognizing that the proposed approaches cannot be considered in the abstract but, rather, must be considered in the context of the magnitude of the need relative to the regulatory principles and efficiency applicable to their implementation.²
9. During the course of the proceeding, three different approaches to community expansion were presented for the Board's consideration:
- (i) ***Internal utility subsidy*** – premised on amendments to EBO 188, this approach was proposed by Union and Enbridge and reflects a rational approach that maintains regulatory principles of continued cost casualty and no undue discrimination while providing for a simple and transparent process that balances the interests of new and existing ratepayers.
 - (ii) ***The status quo*** – this was proposed primarily by competing fuel providers that oppose any change to EBO 188 that would permit a subsidy for the delivery of natural gas services, which approach would therefore not be expected to result in meaningful levels of community expansion.
 - (iii) ***Competition and global subsidization*** – this was proposed primarily by EPCOR and in a manner that under-played this approach's complexity and

² For example, Union's proposal for 29 projects provides access to 18,000 new ratepayers or approximately 1.2% of its existing 1.4 million ratepayers, and 0.5% of the 3.4 million natural gas ratepayers across the province.

the extent to which it represents a departure from regulatory principles such as cost casualty.

10. As set out below, the approach employing a global subsidy is outside the Board's jurisdiction. In any event, considering the proposed approaches on a spectrum, the competition/global subsidization approach is at one extreme resulting in a process that lacks transparency, could result in a proponent distributor with a rate offering that is not in the public interest, and that is administratively burdensome and complex relative to the overall expansion need. At the other extreme is the status quo approach, which is premised on the self-interest of competing fuel providers and does not advance the underlying policy objective, the interests of potential expansion area customers or municipalities, and does not recognize the broader benefits as demonstrated by the Stage 2 economic analysis.³
11. The internal utility subsidy approach proposed by Union strikes a rational balance between the interests of current and future ratepayers, with limited subsidization and minimal rate impacts derived in a transparent manner through an open process, using an existing framework that permits efficient and timely implementation.
12. In the submissions that follow, Union considers:
 - Jurisdictional issues
 - Union's model
 - Status Quo approach
 - Competition and global subsidization
 - Related Issues

³ See Exhibit J4.8 of EB-2016-0004.

B. JURISDICTIONAL ISSUES

(a) *Importance of Understanding Jurisdictional Aspects*

13. As noted, there have been three broad approaches to community expansion proposed in the proceeding, namely (a) amending or granting exemptions from the established EBO 188 framework, (b) maintaining the status quo, and (c) introducing competition for franchise rights together with establishing a global reserve fund and corresponding levy. In considering these approaches, it is essential that the Board do so with a clear understanding of its jurisdiction to implement each approach. While the proposal to maintain the status quo and the proposal to amend/grant exemptions from the EBO 188 framework do not raise jurisdictional concerns, significant concerns are raised by the proposal to introduce competition for franchise rights and establish a global reserve fund. These are important threshold issues that will impact the resolution of a number of other issues in this proceeding.
14. In Union's view, the Board does not have authority to establish a framework where the customers of one distributor subsidize expansion undertaken by another distributor into unserved communities. Moreover, the Board does not have authority to establish a global reserve fund or impose a corresponding general levy. However, the Board does have authority to permit limited internal utility cross-subsidization consistent with the broad framework established in EBO 188. These aspects are considered in the sections below.

(b) *Board has No Jurisdiction to Permit Subsidization on Inter-Utility Basis*

15. Administrative tribunals obtain their jurisdiction either by express grant or by application of the doctrine of jurisdiction by necessary implication. With respect to an express grant, the *Ontario Energy Board Act, 1998* (the "Act") does not expressly provide that in setting just and reasonable rates the Board shall or may establish a mechanism by which the customers of one gas distributor subsidize the customers of another gas distributor. The Board's jurisdiction for setting gas distribution rates is largely established by s. 36 of the Act, ss. (3) of which provides that, in approving or fixing just and reasonable rates, the Board may adopt any method or technique that it considers appropriate. The Board is

therefore granted broad discretion in setting rates, so long as the rates that it sets are in accordance with the just and reasonable standard (discussed below).

16. The doctrine of jurisdiction by necessary implication provides that the powers conferred by an enabling statute are to be construed so as to include not only those expressly granted but also, by implication, all powers which are practically necessary for the accomplishment of the object intended to be secured by the statutory regime created by the legislature.⁴ The circumstances when the doctrine may be applied are when:

- the jurisdiction sought is necessary to accomplish the objects of the legislative scheme and essential to the tribunal fulfilling its mandate;
- the enabling legislation fails to explicitly grant the power to accomplish the legislative objective;
- the mandate of the tribunal is sufficiently broad to suggest a legislative intention to implicitly confer jurisdiction;
- the jurisdiction sought is not one which the tribunal has dealt with through use of expressly granted powers, thereby showing an absence of necessity; and
- the legislature did not address its mind to the issue and decide against conferring the power upon the tribunal.⁵

17. In Union's view, the above-listed circumstances do not present themselves in respect of the proposal for inter-utility subsidization. The Board does not require authority to approve inter-utility cross-subsidization in order to accomplish the objects of the legislative scheme or to fulfill its mandate under the Act. As Union's proposal shows, the Board can accomplish its objects and fulfill its mandate without that authority. Moreover, while the Board has broad jurisdiction in fulfilling its mandate, a key constraint on the Board is that rates are to be set in accordance with the just and reasonable standard, which as further discussed below does not support subsidization of one utility by another. In addition, in the very limited circumstances where the Board has previously permitted inter-utility cross-subsidization, it has done so only on the basis of

⁴ *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] 1 S.C.R. 140, 2006 SCC 4 (CanLII) at para 51.

⁵ *Toronto Hydro-Electric System Ltd. v. Ontario (Energy Board)*, 93 OR (3d) 380, 2008 CanLII 89827 (ON SC) at para 49.

expressly granted powers. In one of those circumstances, the legislature expressly granted powers for the Board to approve inter-utility subsidization to support rural and remote ratepayers in respect of electricity costs, but the legislature did not extend that power to the Board in respect of gas ratepayers.

18. Given that the legislature turned its mind to the issue of inter-utility subsidization for the benefit of utilities that serve rural and remote energy customers, and that the legislature decided against conferring this power on the Board in respect of gas services, the Board should not be found to now have that power by necessary implication. This aspect is significant because of the fact that the legislature has previously established general subsidy arrangements through frameworks for rural and remote ratepayer protection for electricity customers under s. 79 of the Act and for rate assistance under ss. 79.2 of the Act. The frameworks under s. 79 and s. 79.2 are the only instances in the Act where the legislature requires or has permitted the Board to require the costs of some utilities to be borne by the customers of other utilities.
19. Under the s. 79 framework, the Board, in approving just and reasonable rates for electricity distributors that serve rural and remote areas, is required to provide rate protection for rural and remote customers by reducing the rates that would otherwise apply. The distributor, in turn, is entitled to be compensated for lost revenue resulting from the rate protection. Subsection 79(3) provides that “all consumers (in Ontario) are required to contribute towards the amount of any compensation” payable to the distributor. Under this framework, the Board is required by the legislature to ensure amounts are collected through distribution rates from all consumers and paid to those distributors that serve rural and remote customers in order to subsidize the cost of serving those customers. This regime recognizes that there is generally a higher cost involved in serving energy customers that are situated in rural and remote areas because of the infrastructure needed to reach those customers and the lower numbers and densities of customers over which to spread the costs of that infrastructure. Having considered these

circumstances, the legislature decided to require the Board to implement a rate protection scheme based on the parameters set out in the Act.⁶

20. The inclusion of the s. 79 framework in the Act demonstrates that the legislature turned its mind to the issue of providing rate subsidization for energy consumers in rural and remote areas, but that it decided only to provide such protection for customers of electricity distributors and not to provide such protection for customers of gas distributors. Moreover, the fact that the legislature saw a need to enact s. 79 so as to empower the Board to provide rural and remote rate protection for electricity distribution customers indicates that the legislature recognized it had not expressly granted such powers to the Board under the Act, and was of the view that the Board did not have those powers by necessary implication. The legislature evidently reached a similar conclusion in expressly granting powers to the Board under s. 79.2 so that the Board could implement a rate assistance program that requires inter-utility subsidization.
21. In Union's view, express authority to establish an inter-utility subsidization regime is required because, in the absence of such authority, rates would not be established in accordance with the just and reasonable standard that currently applies under the *Ontario Energy Board Act*. The Supreme Court of Canada recently summarized the just and reasonable standard of rate regulation as follows:

In Canadian law, “just and reasonable” rates or tariffs are those that are fair to both consumers and the utility: *Northwestern Utilities Ltd. v. City of Edmonton*, [1929 CanLII 39 \(SCC\)](#), [1929] S.C.R. 186, at pp. 192-93, per Lamont J. Under a cost of service model, rates must allow the utility the opportunity to recover, over the long run, its operating and capital costs. Recovering these costs ensures that the utility can continue to operate and can earn its cost of capital in order to attract and retain investment in the utility: *OEB*, at para. 16. Consumers must pay what the Commission “expects it to cost to efficiently provide the services they receive”

⁶ The s. 79.2 framework works similarly in that distributors who serve customers that qualify for rate assistance are entitled to compensation for lost revenue, which amounts are paid for by all distribution consumers in Ontario through amounts added to their rates.

such that, “overall, they are paying no more than what is necessary for the service they receive”: *OEB*, at para. 20.⁷

22. If the approved rates that one utility charges its customers include amounts used to fund a subsidy for another utility, that portion of the first utility’s rates would not be based upon any underlying costs incurred by that utility to serve its customers. Rather, that portion of the first utility’s rates would be based on the costs incurred by the second utility to serve the second utility’s customers. To the extent that the first utility’s rates are based upon costs unrelated to the regulated service that it provides, such rates would not be in accordance with the just and reasonable standard. To paraphrase the Supreme Court of Canada, the first utility’s customers would pay more than what is necessary for the service they receive.
23. As described in Union’s pre-filed evidence (Ex A, Tab 1, pp. 3-5), a regime of inter-utility subsidization would also offend several fundamental rate-making principles:
- The “benefits follow cost” principle establishes that consumers should bear only the costs for which they are responsible.⁸ Under a regime of inter-utility subsidization, one utility’s customers would be incurring costs without receiving any corresponding benefits and, on the flip side, the other utility’s customers would be receiving benefits without incurring any corresponding costs.
 - The “stand-alone” principle holds that only those costs and risks that pertain to the activities of a regulated utility in respect of the provision of service to ratepayers should be reflected in the revenue requirement of that utility.⁹ To charge one utility’s customers an amount that would be used as a subsidy for another utility would be to include in the first utility’s revenue requirement costs that are unrelated to the activities of that first utility. Alternatively, if those amounts do not form part of the first utility’s revenue requirement but are recovered in rates, then those amounts would be incremental to that utility’s revenue requirement and rates established would recover more than the utility’s revenue requirement in a manner contrary to the just and reasonable standard.
 - The “fair return standard” has been described by the Supreme Court of Canada as meaning “that the company will be allowed as large a return on the capital invested in its enterprise, which will be net to the company, as it would receive if

⁷ *ATCO Gas and Pipelines Ltd. v. Alberta (Utilities Commission)*, 2015 SCC 45 at para 7.

⁸ R. Hahne and G. Aliff, *Accounting for Public Utilities*, 17.05[2], p. 17-43, October 2009.

⁹ K. McShane, *Report on The Disposition of Tax Savings on Disallowed Expenses, Submitted on behalf of the Coalition of Issue Three Distributors*, EB-2004-0188, January 12, 2005 at para 5.

it were investing the same amount in other securities possessing an attractiveness, stability and certainty equal to that of the company's enterprise."¹⁰ The basis of a fair return is the amount of capital invested by the shareholder in its enterprise. It would be contrary to this standard, and the just and reasonable standard, if the utility undertaking expansion were permitted, through the rates it charges to its own customers, to earn a return on the portion of its rate base that, if subsidization is permitted, would effectively have been paid for by the ratepayers of one or more other utilities. As such, if a regime of inter-utility subsidization is implemented, the utility that receives subsidization should have a corresponding reduction in its rate base or return.

24. Based on the foregoing, the Board does not, either by express grant or by necessary implication, have authority to establish a framework under which the customers of one gas distributor may or are required to subsidize expansion undertaken by another distributor to serve a new community that is otherwise unserved. The Board does not have this authority to establish such a framework in the context of a consultation process or generic proceeding, nor does the Board have this jurisdiction in the course of setting gas distribution rates. To do so would be contrary to the Board's obligation to establish rates in accordance with the just and reasonable standard and would offend fundamental ratemaking principles. Consequently, a regime of inter-utility subsidization could only be implemented based on an express grant of legislative authority demonstrating a clear intention on the part of the legislature, consistent with the approach taken under s. 79.2 of the *Ontario Energy Board Act*.

(c) *Board has No Jurisdiction to Establish Global Reserve Fund or Levy*

25. With respect to the proposal to establish a global reserve fund and corresponding levy for community expansion, Union submits that the Board does not have the jurisdiction to do so absent express legislative authority. The reasons set out in the above discussion concerning jurisdiction to implement inter-utility subsidization are also generally applicable to the question of whether the Board has jurisdiction to establish a global reserve fund and levy. The Board has no express grant of authority to establish such a fund, nor does it have such authority by necessary implication. We note that there is no principled difference between improperly requiring the cost of subsidizing a community

¹⁰ *Northwestern Utilities Limited v. City of Edmonton*, [1929] S.C.R. 186.

expansion project of one distributor to be borne by the customers of another distributor, and the circumstance where the subsidy cost is borne by the customers of all other Ontario distributors through a global levy. Having regard to the circumstances under which a tribunal may be found to have jurisdiction by necessary implication, Union notes that given the range of approaches being considered in this proceeding it is not necessary for the Board to establish a global reserve fund and levy to accomplish its legislative objective of facilitating the rational expansion of gas distribution. The Board can achieve this objective through other means that are within its authority to set just and reasonable rates.

26. In addition, Union supports the argument of Canadian Propane Association (“CPA”) that the Board has no jurisdiction to impose a province-wide natural gas subsidy because it would effectively be a tax (see CPA’s pre-filed evidence, pages 4 to 6). CPA bases its argument on the fact that the proposed global levy would not be a charge for services rendered but rather a tax to raise revenue for a general purpose, and that any delegation of the legislature’s power of taxation must be clear and unambiguous. Union generally agrees with this characterization as it applies to a province-wide subsidy, and also references the decision in *Advocacy Centre for Tenants-Ontario v. Ontario Energy Board* (2008), 293 D.L.R. (4th) 684 (“Advocacy Centre”), where the Ontario Divisional Court similarly explains, at para. 46:

If the Board were to reduce the rates for one class of consumers based upon an income determinant, the Board would have to increase the rates for another class or classes of consumers. In effect, such a rate reduction would impose a regressive indirect tax upon those required to pick up the shortfall. Such an approach would arguably be a dramatic departure from the Board’s regulatory function as implemented to date, which has been to protect the collective interest of consumers dealing with a monopoly supplier through a “cost of service” calculation and then to treat consumers equally through determining rates to pay for the “cost of service” on a cost causality basis for classes of consumers.

27. The court in *Advocacy Centre* goes on to say that the Board is an economic regulator rather than a formulator of social policy, which is a function of the elected legislature. In this regard, the court cited an example of a previous program under provincial income tax

legislation for the purpose of providing for public tax expenditures to assist low income consumers with electricity costs (See Advocacy Centre, paras. 47-49).

28. Therefore, unless clearly authorized by legislation, the Board lacks the authority to establish the proposed global reserve fund and corresponding levy, which would effectively be a tax imposed on all ratepayers to assist new customers with community expansion costs in support of the provincial policy goal of encouraging community expansion.

(d) Board May Allow Limited Intra-Utility Subsidization

29. It is not possible to eliminate cross-subsidization entirely – it is implicit where postage stamp rates are applied to multiple customers. In light of the Province’s desire to support expansion to new communities and the Board’s request for proposals which indicated a willingness to consider reduced Project PIs, Union submits that it would be in the public interest to allow limited levels of intra-utility cross-subsidization. This would fall within the scope of the Board’s jurisdiction provided that long-term rate impacts are reasonable and principles of cost causation are, to the extent possible, adhered to. This would be consistent with the approach taken by the Board in EBO 188, where the portfolio approach was found to be in the public interest notwithstanding that it would permit some projects to proceed that, on a stand-alone basis, would not be financially feasible. Implicit in the portfolio approach is that some of a utility’s customers would be subsidizing other customers of that utility.

C. UNION GAS MODEL

30. In response to the Minister’s Letter and the Board’s February 18, 2015 invitation, Union filed an application and evidence on July 23, 2015 for the expansion of its natural gas distribution network to a number of unserved communities across Ontario (EB-2015-0179). By way of Procedural Order No. 1 in the current proceeding, Union’s evidence in EB-2015-0179 was made part of EB-2016-0004. In the context of the present generic proceeding, Union continues to view its Community Expansion Proposal set out in EB-2015-0179 as the preferred approach that should be adopted by the Board.

(a) *Description of Model*

31. Union's Community Expansion Proposal provides flexibility to the EBO 188 guidelines to enable expansion to communities that would not otherwise receive natural gas service based on a strict application of those guidelines. Union's proposed approach considers those who will be impacted by and who will benefit from expansion, and strives to find an appropriate balance in terms of how the impacts will be borne by different stakeholders commensurate with the benefits received. Accordingly, Union's Community Expansion Proposal is a principled approach consistent with the following:

- Customers and municipalities who directly benefit from Community Expansion Projects should contribute to the financial viability of the project;
- Expansion customer contributions to project feasibility should be commensurate with the savings achieved by switching to natural gas;
- Moderate cross-subsidization from existing customers is acceptable, provided long term rate impacts are reasonable; and
- Natural gas distributors should not be exposed to financial risk related to the incremental new community capital investments.

32. Building on these principles, Union's Community Expansion proposal is comprised of three key elements:

- (a) allowing for supplemental revenues through (a) a temporary surcharge payable by customers served by Community Expansion Projects, and (b) a mechanism for municipalities to contribute toward the feasibility of Community Expansion Projects;
- (b) applying lower minimum economic feasibility thresholds through (a) an exemption from the minimum project PI threshold established in EBO 188 for Community Expansion Projects, and (b) an exemption from the requirement established in EBO 188 for Community Expansion Projects to be included in both the distribution Investment Portfolio and the Rolling Project Portfolio; and
- (c) deferral accounts to assist in administering the process, including (a) a deferral account to capture the temporary customer surcharges and municipal contributions, which would then be disposed of to ratepayers to reduce cross-subsidization, and (b) a deferral account to capture variances between the forecast net revenue requirement approved in rates and actual revenue requirement for

Community Expansion Projects, which would then be disposed of to ratepayers in proportion to the allocation of project costs to rate classes.

Each of these interconnected elements of Union's Community Expansion Proposal, as well as the corresponding benefits, are described in greater detail below.

(a) Supplemental Revenues

(i) *Temporary Expansion Surcharge*

33. Union's approach includes the introduction of a volumetric Temporary Expansion Surcharge ("TES"), which would be charged to general service customers that convert to natural gas in order to be served by a Community Expansion Project. For transparency and simplicity, the TES would be charged as a line item on a customer's monthly bill and be applicable for a defined period of time to permit a customer contribution to the cost of the Community Expansion Project. Amounts collected from the TES would be recorded in a deferral account and disposed of annually to ratepayers to offset cross-subsidization, thereby striking a balance between new and current customers and adhering to the regulatory principle of avoiding undue discrimination.
34. The amount of the surcharge, as described in EB-2015-0179, would be \$0.23/m³. A TES at the proposed rate of \$0.23/m³ is equal to an annual cost of \$506 for a typical residential customer. Based on assumptions set out by Union in EB-2015-0179¹¹, even after paying the surcharge, on average, customers will have annual savings that allow them to pay back their cost of conversion to natural gas in 4.8 years. After the initial 4.8 year payback period, the customer would see annual savings of \$1,061 until the TES is terminated, after which savings would increase to \$1,567 per year. With the TES set at this level, the customer can contribute to the Community Expansion Project while still achieving savings in years 1 to 5, with increased savings after year 5 and further increased savings after expiry of the TES. The duration over which the TES will be applied will vary from project to project based on the period of time needed to reach the

¹¹ EB-2016-0004, Exhibit S15.Union.SEC.5

minimum PI for each project, but would not exceed 10 years from the date the project goes into service.

(ii) Incremental Tax Equivalent Mechanism

35. Union’s Community Expansion Proposal also includes the introduction of a municipal contribution mechanism or the Incremental Tax Equivalent (“ITE”), to enable municipalities to contribute towards the feasibility of Community Expansion Projects. The ITE value would be based on the estimated value of incremental property taxes collected from Union as a result of the project for a time period that matches the TES term. The ITE would be implemented by way of an agreement between Union and the relevant municipality prior to commencing construction, where that municipality chose to pursue Community Expansion Projects at reduced economic threshold levels below a PI of 0.8. As with the TES, amounts collected through the ITE would be recorded in a deferral account and disposed of annually to ratepayers.

(b) Lower Minimum Economic Feasibility Thresholds

(i) Exemption from PI Threshold for Individual Community Expansion Projects

36. As part of Union’s Community Expansion Proposal, the Board would exempt Community Expansion Projects from the minimum economic threshold established in the EBO 188 framework, being a PI of 0.8, and allow for a lower minimum economic threshold of 0.4. This lower threshold would apply only to projects that meet Union’s proposed definition of a “Community Expansion Project”, where customers to be served by the project will be required to pay a TES for at least 4 years and where the relevant municipality agrees to make ITE contributions for the term of the TES. Union defines “Community Expansion Projects” as system expansion projects that will provide first-time natural gas system access where a minimum of 50 potential customers in homes and businesses already exist, for which minimum economic feasibility guidelines permit a profitability index of less than 1.0.
37. To strike a balance, the proposed lower threshold, of a PI of 0.4, has been determined by Union based on analysis of potential projects, and with a view to achieving an

appropriate balance between furthering the provincial policy objective of providing customers in non-serviced communities with the ability to gain access to natural gas, and being mindful of the potential rate impacts for existing ratepayers. Whereas a minimum PI of 0.4 would enable Union to undertake 29 projects to serve over 18,000 potential customers in 33 communities, a higher minimum PI of 0.5 would only enable Union to undertake 20 projects to serve nearly 8,000 potential customers in 21 communities and a minimum PI of 0.6 would reduce these numbers further. In the other direction, Union found that a PI of 0.3 would result in expected rate impacts approaching \$2 per month, which as discussed below is the maximum rate impact under Union's Community Expansion Proposal. Moreover, there would be a significant escalation in incremental capital costs per customer if the minimum project PI was reduced below 0.4.

(ii) *Exemption from Investment Portfolio and Rolling Project Portfolio Requirements for Community Expansion Projects*

38. Union's proposal provides further regulatory flexibility by means of an exemption from the EBO 188 requirements that Community Expansion Projects be included in both the distribution Investment Portfolio ("IP") and the Rolling Project Portfolio ("RPP"). Without these exemptions, allowing a lower minimum project PI for individual Community Expansion projects would have a very limited impact on Union's ability to expand and to serve additional communities unless the IP and RPP limitations are also addressed. Otherwise, the lower economic thresholds allowed for individual projects would drive the IP down below the established minimum requirement. Union notes that, in the EBO 188 Final Report, the Board indicated that it would be prepared on an exception basis to consider a utility submission as to why a proposed project should not be included in the portfolio but treated separately.¹² As such, the EBO 188 framework already contemplates providing the type of regulatory flexibility that is contemplated by this aspect of Union's proposal.

¹² EBO 188 Final Report of the Board, dated January 30, 1998, Section 2.1.2.

(c) Deferral Accounts

39. The final component of Union’s proposal involves establishing two deferral accounts, which will enable the process to be implemented efficiently through existing regulatory mechanisms.

(i) Community Expansion Project Deferral Account

40. A “Community Expansion Project Deferral Account” would be established for the purpose of recording variances between the forecast net revenue requirement approved in rates and actual revenue requirement for all Community Expansion Projects, including timing differences between the in-service dates and inclusion in rates. Balances in this account would be disposed of as part of Union’s annual non-commodity deferral account disposition proceeding. Balances would be disposed of to ratepayers in proportion to the allocation of Community Expansion Project costs to rate classes.

(ii) Community Expansion Contribution Deferral Account

41. A “Community Expansion Contribution Deferral Account” would be established for the purpose of recording TES contributions from customers and ITE contributions from municipalities. Generally, the purpose of this deferral account is to allocate the TES and ITE revenues to ratepayers to reduce the cross-subsidization of capital costs. Balances in this account would be disposed of as part of Union’s annual non-commodity deferral account disposition proceeding. TES amounts would be allocated to all ratepayers based on the same allocation as the Community Expansion Project capital costs in rates. ITE amounts would be allocated to ratepayers based on Union’s Board-approved property tax allocation.

(b) Rate Consequences

42. Union’s proposal would enable it to complete 29 projects to serve 33 new communities at a capital cost of approximately \$135 million. The rate consequences of this proposal are reasonable for both new connecting customers and existing customers. For new connecting customers, the TES would be set at a level that enables them to enjoy a small amount of overall savings during an initial payback period of 4.8 years, after which a

typical new residential customer would see overall savings of \$1,061 while still paying the TES and \$1,567 after the TES expires. For existing customers, as explained in Exhibit B.Staff.9 in EB-2015-0179, Union proposes that any increase in rates resulting from Community Expansion projects in a given year be limited to a maximum of \$10 for a typical residential customer and, to address concerns with the cumulative impacts of a multi-year expansion program, the cumulative impact for a multi-year period be limited to a ceiling of \$24 per year (average of \$2 per month) relative to rates that would have existed absent a Community Expansion Program. Net of the TES and ITE deferral account credits, the expected peak rate impact for existing customers of Union's proposal, comprised of 29 projects to serve 33 new communities, would be \$2.91 per year or \$0.24 per month for a typical residential customer (Transcript Vol. 4, p. 172). This is significantly less than the proposed ceiling of \$2 per month.

(c) ***Benefits of Approach***

43. Union's Community Expansion Proposal advances the provincial policy objective of expanding natural gas service to new communities, while limiting the rate impacts on existing consumers to a reasonable level. Moreover, Union's approach can be implemented and administered through established regulatory processes and generally within the existing framework established in EBO 188. In addition, each of the individual elements of Union's proposal have been developed on the basis of sound regulatory principles.
44. The TES ensures that those customers that will benefit from expansion will also bear a share of the costs of expansion. In addition, the TES is designed so that customer contributions to project feasibility will be commensurate with the savings that the customer will realize by switching to natural gas. The TES also helps overcome several key barriers to community expansion, including the economic feasibility of expansion projects, the initial financial burden presented by traditional up-front contributions in aid of construction, and potential customers delaying conversion so as to avoid the up-front costs of paying a contribution in aid of construction. In addition, by setting the TES at a level that enables a new customer to enjoy a small cost savings in the short-term (during

the initial payback period), followed by larger cost savings over the medium-term (while the TES is in place) and even greater savings in the long-term (after the TES expires), Union's proposed approach is expected to be attractive to a significant portion of potential customers and result in significant uptake.

45. The ITE enables municipalities to contribute toward project feasibility, consistent with the principle that the beneficiaries of expansion should contribute towards the financial viability of the project. Municipalities will benefit from the elimination of a key barrier to economic development, as well as incremental property taxes from the projects (without corresponding increases in the costs of delivering municipal services). In addition, many municipalities will benefit from reduced energy costs for municipally-owned facilities.
46. The exemption from the minimum project PI threshold of 0.8 established in EBO 188, and application of a minimum project PI of 0.4 to Community Expansion Projects, would enable a reasonable balance between the provincial policy objective of expanding service to new communities and the need to minimize the cost impacts for existing ratepayers to be achieved. The exemption from IP and RPP requirements established in EBO 188 would enable the benefits of the first exemption to be fully realized. Together, these exemptions and their resulting rate impacts provide for an approach that is consistent with the principle that cross-subsidization from existing customers is acceptable, provided that the long-term rate impacts are reasonable. Moreover, given that the Board in EBO 188 expressed a willingness to consider circumstances where exemptions from EBO 188 requirements would be appropriate, Union's proposal is consistent with the overall regulatory framework established by the Board in that proceeding.

(d) *Implementation*

47. As alluded to above, one of the key benefits of Union's Community Expansion Proposal is its relative ease of implementation and efficiency from a regulatory perspective. The Board already has the necessary jurisdiction to give effect to Union's proposed approach - no legislative or regulatory changes are needed. The proposal operates within the general framework established in EBO 188, with which the Board and key stakeholders

are already familiar, and seeks exceptions that are of a nature that were contemplated by the Board at the time it established the EBO 188 guidelines. Moreover, the proposal can be administered and overseen by the Board through established rate-setting and implementation practices. For example, Union would seek to dispose the balances in the proposed deferral accounts as part of its existing annual non-commodity deferral account disposition proceeding. Also notable is that the proposed approach would be transparent. For example, new customers would see the TES as a line item on their bill and existing customers would over time be able to see that the TES and ITE amounts collected by Union are being credited back to them through the deferral account disposition process.

48. As described by Union's witness panel (Transcript Vol. 4, p. 172), implementation would begin with a s. 36 rate application, as well as a s. 90 leave to construct application (if necessary), which would allow parties and the Board to review capital costs and the demand forecast supporting a project. Once approved, the project would be implemented in rates through Union's annual rate-setting process. During the term of the project, amounts would be recorded in the deferral account to account for differences between actual and forecast capital costs. In addition, during Union's annual stakeholder review it would track and report, on a project-by-project basis, the capital costs associated with each project, any upfront contributions in aid of construction, the net capital included in rates, the applicable term for the TES and ITE, as well as the forecast and actual level of attachments.

D. COMPARISON OF UNION AND ENBRIDGE APPROACHES

49. Union is proposing to spend \$135 million to provide access to natural gas service for approximately 18,000 homes and businesses, and expects about 50% of those customers to convert in the first ten years. Enbridge is proposing to spend \$410 million to provide access to natural gas service for approximately 20,500 consumers and expects about 75% of those customers to convert in the first ten years. The similarities and differences between the proposals were described by Union's witness panel (Transcript Vol. 4, pp. 173-175) and are summarized below.

50. The proposals from both Union and Enbridge rely upon a common definition of a “Community Expansion Project”, which is one that provides access to natural gas service to a minimum of 50 existing homes and businesses. Both proposals include volumetric temporary surcharges for expansion area customers set at \$0.23/m³ and both proposals include an incremental tax equivalent mechanism to allow for municipal financial support. Both proposals also include exemptions of Community Expansion Projects from the current EBO 188 investment portfolio requirements and both propose a maximum allowable net rate impact resulting from a broad community expansion program to be capped at \$2/month for an existing typical residential customer. Moreover, both the Union and Enbridge proposals include a capital pass-through mechanism.
51. Whereas Union proposes that the TES would be set for a period ranging from 4-10 years, Enbridge proposes that the TES be set at the lesser of 40 years or the period of time it takes for a project to reach a PI of 1.0. In addition, while Union would only apply the TES to general service customers in an expansion area, Enbridge would apply it to all expansion area customers. With respect to the ITE, Union proposes that it be mandatory for projects with a PI of less than 0.8 and apply for a period ranging from 4-10 years depending on project economics, while Enbridge would require an ITE for projects with a PI of less than 1.0 and apply it for a period of 10 years in all cases.
52. In terms of minimum economic feasibility thresholds, whereas Union has proposed a minimum project PI of 0.4, Enbridge proposes that there be no minimum. As a result, while Union has limited its initial list of potentially feasible projects to 29 of approximately 100 possible projects, Enbridge would regard all identified projects as potentially feasible. Consequently, Union’s proposal is of a smaller scale than Enbridge’s and while the rate impact of Union’s proposal for a typical residential customer would peak at \$0.24/month, the rate impact of Enbridge’s proposal for a typical residential customer would peak at \$0.87/month. Moreover, while Union would have Community Expansion Projects exempted from the EBO 188 RPP requirement and instead manage to a rate ceiling impact of \$2/month, Enbridge would group all Community Expansion Projects into a separate portfolio and manage it to a minimum PI of 0.5 along with a \$2/month ceiling.

E. STATUS QUO

53. Ontario natural gas utilities are required to comply with the Board's EBO 188 guidelines for the expansion of natural gas services. In essence, EBO 188 supports an approach that is intended to facilitate the expansion of natural gas service while adhering to the key principle that existing ratepayers ultimately should be held harmless from rate impacts resulting from the cost of new connections.

54. Although the key principles which underlie the EBO 188 approach have served the industry and most ratepayers well, it was implemented during a period that preceded the recent provincial policy goal of providing customers in unserved communities with more energy choices. This policy goal cannot be achieved without some form of cross-subsidization. Alternative fuel providers, who serve those areas not served by natural gas, oppose this result and seek to maintain the status quo to the detriment of unserved communities and the environment.

(a) *Outside Scope of Minister's Letter*

55. Maintaining the status quo would not support the objectives set out in the Minister's Letter of February 17, 2015 including in particular the province's commitment in the LTEP to work with distributors and municipalities to pursue options for expanding natural gas service to communities in rural and northern Ontario. The Minister specifically asked the Board to move forward on a timely basis to consider opportunities to facilitate access to natural gas services for more communities through the rational expansion of gas transmission and distribution systems in Ontario, in line with the province's commitment to that objective.

56. If the Board were to determine that the current framework established under EBO 188 should continue to apply in its present form to Community Expansion Projects, the Board would not be facilitating access to gas service to more communities but, rather, would be ensuring that access to natural gas service remains largely out of reach for all communities in Ontario that are currently without access. As described by Union's witness panel, and as echoed by Enbridge's witness panel, many prospective consumers

are seeking access to natural gas and gas distribution services. However, when the EBO 188 requirements are applied to Community Expansion Projects, the projects are typically found to be uneconomic and the required contribution in aid of construction is found to be more than consumers are willing to pay (Transcript Vol. 4, pp. 166-167). Despite these circumstances, over the past 10 years Union has attached over 43,000 customers through conversions within or immediately adjacent to its existing serviced areas. However, over this same period Union has only expanded to one new community requiring Board facilities approval (EB-2015-0179, Ex A, Tab 1, pp. 11-12). This demonstrates that continuing with the status quo will not result in the expansion of gas distribution service to new communities consistent with provincial policy objectives.

(b) Cost Differential

57. If the existing framework is maintained, which as noted would have the effect of forestalling the expansion of gas service to new communities, consumers in unserved rural and northern Ontario communities would need to continue their reliance on more costly energy sources. As described in Ex S15.Union.Energy Probe.15(d) in EB-2016-0004, whereas the estimated annual cost of energy for a typical residential customer using natural gas would be \$844, the equivalent cost would be \$2,058 for a customer using propane, \$2,554 for a customer using furnace oil and \$3,338 for a customer using electricity on a time-of-use basis. Even when conversion costs are accounted for, access to natural gas service can provide significant savings for energy customers. Moreover, since 2006 the annual cost of natural gas has decreased by 31% whereas the annual cost of propane, furnace oil and electricity has increased by an average of 38%.¹³ If these trends continue, the cost differential between natural gas and other energy sources would continue to grow.

(c) Environmental Impacts

58. In addition to the higher costs for consumers that do not have access to natural gas, maintaining the existing framework for community expansion would have environmental

¹³ EB-2015-0179, Exhibit A, Tab 1 (Update), pp. 9-10.

implications. This is because natural gas usage results in lower greenhouse gas emissions than other fossil fuels, such as propane and furnace oil, which would be displaced with increased access to natural gas. As noted in response to Exhibit B.CCC.5 in EB-2015-0179, Union's Community Expansion Proposal would result in greenhouse gas emissions reductions of nearly 7,700 tonnes of CO₂ equivalent each year. In addition, as described in response to Exhibit B.SEC.10 in EB-2015-0179 based on more detailed analysis of the environmental impacts of four particular proposed projects, gas conversion would be expected to result in an approximately 8% reduction in greenhouse gas emissions relative to the existing fuel mix in unserved communities, plus conversion would result in significant reductions in emissions of particulate matter (79%) and sulphur dioxide (81%). As provincial policies seek to incorporate the price of carbon into energy prices, it is expected that the lower greenhouse gas emissions from natural gas will in turn result in the cost of natural gas increasing by at least that of the cost increases that will be seen for other fossil fuel-based energy sources.

(d) Based on Commercial Self-Interest of Service Provider

59. To the extent that parties express support for maintaining the status quo, such parties are doing so solely in their commercial self-interest and with little regard for provincial policy objectives, the cost impacts for Ontario's energy customers, the economic impacts on communities that are currently without access to natural gas service, and the broader environmental implications of forestalling conversions to natural gas.

F. COMPETITION / GLOBAL SUBSIDY

(a) Competition

60. At the core of EPCOR's proposal for community expansion is competitive franchise bidding as a mechanism to achieve the expansion of distribution services to underserved communities. At a highly theoretical level, Dr. Adonis Yatchew (testifying on behalf of EPCOR) hypothesized that competition for franchise opportunities would provide the lowest cost result with respect to capital cost. He provided no empirical analysis to substantiate this assertion. Instead, he relied on the purely theoretical premise that if there

is more than one party participating in the bid, the lowest cost would result. However, Dr. Yatchew's supposition is flawed because it does not take into account (i) the terms and conditions of the selection process, and (ii) the goals and objectives of the initiator of the competitive process. Both of these factors have a direct application on the outcome of such a process and whether the public interest is achieved by completing such process. In fact, in certain circumstances following a competitive franchise selection process, the Board could be pre-empted from ensuring that the public interest is protected as part of its determination in a franchise or leave to construct proceeding.

61. During cross-examination Dr. Yatchew readily agreed that a competitive process' selection criteria and the weighting of that criteria will directly affect both who participates and who is ultimately selected by virtue of the process.¹⁴ If the municipality, as the initiator of the competitive process, has goals and objectives that are focused on aspects other than the rates or capital cost levels such as some other municipal benefit, then it is likely that the end result of the competitive process will not be the lowest cost. Similarly, if the criteria for selection involves providing a service to the municipality in addition to the provision of gas distribution, then the number or type of participants in the preceding may be limited and the best or highest quality natural gas distribution service may not necessarily be acquired by virtue of the competitive process.
62. For example, in the recent competitive process undertaken by South Bruce¹⁵, the municipality had no understanding as to the rate impacts associated with their selection.¹⁶
63. The South Bruce procurement process also resulted in a franchise arrangement with EPCOR in which EPCOR would pay an annual fee to South Bruce representing 1% of gross revenues. Using this example as a basis, the important aspect for the Board to consider in the context of a competitive process and any inducement paid by participant, is that the competitive process may be more about the inducement provided by a bidder to the municipality than the broader public interest of serving the ratepayer.

¹⁴ EB-2016-0004, Transcript Vol. 7, pp. 44-45.

¹⁵ Municipalities of Kincardine, Arran-Elderslie and Township of Huron-Kinloss.

¹⁶ Exhibit S.13, South Bruce, p. 24,

64. Moreover, to the extent that such inducement fees are in addition to the normal municipal taxes and the municipality's reasonable cost for issuing permits, they not only have a negative impact on the competitive process and are anti-competitive, but are also contrary to the Board's past decisions on this issue as well as the *Municipal Act*.
65. The Board has consistently held that Franchise Agreements should not include terms or conditions that provide for the payment of franchise fees by a utility to a municipality. The Board reached this conclusion in a series of decisions and reiterated its position on this issue in the proceeding that gave rise to the 1987 Model Franchise Agreement (E.B.O. 125). Further, the Board did not depart from this approach in the proceeding that gave rise to the 2000 Model Franchise Agreement (RP-1999-0048):
- In E.B.O. 125, the Board initiated a hearing to consider a range of concerns in respect of Franchise Agreements. The final Report of the Board dated May 21, 1986 included references to past Board decisions which held that franchise fees are not in the public interest and that the Board – not the municipality – is the final arbiter in determining the terms and conditions of a Franchise Agreement.¹⁷
 - In RP-1999-0048, the Board considered proposed changes to the 1987 Model Franchise Agreement. The Board also considered the extent of its jurisdiction to govern the relationship between a municipality and a gas utility in light of new *Municipal Act* provisions, which authorized a municipality to pass fee by-laws subject to certain limitations. Those provisions are substantially the same as s. 391 and s. 394(1)(e) of the current *Municipal Act*. According to s. 394(1)(e), “no fee or charge by-law shall impose a fee or charge that is based on, is in respect of or is computed by reference to, ... (e) the generation, exploitation, extraction, harvesting, processing, renewal or transportation of natural resources.” In this regard, the Board concluded that the municipality's authority to pass by-laws imposing fees does not restrict the Board's jurisdiction to determine the terms and conditions governing the relationship between the parties, and that municipalities may only impose permit fees on utilities for activities authorized by a Franchise Agreement if the fees are for recovery of the reasonable costs of administering the permit.
66. Based on the above decisions and s. 394(1)(e) of the *Municipal Act*, if a municipal by-law approves a proposed Franchise Agreement that contains a fee or charge based on and in respect of the transportation (including distribution) of natural resources (namely gas), such by-law would be invalid. Moreover, the current *Municipal Act* includes an

¹⁷ See Board decisions in E.B.A. 304, E.B.A. 316, and E.B.A. 352.

additional limitation, not considered in RP-1999-0048, on the municipality's ability to impose a fee in relation to natural gas. Section 395 of the *Municipal Act* provides that "Nothing in this Act authorizes a municipality or local board to impose a fee or charge for supplying natural and artificial gas which exceeds the amount for the supply permitted by the Ontario Energy Board". This provision affirms the Board's jurisdiction on this issue, such that a municipality may not impose a fee or charge in relation to the supply of natural gas if that fee or charge is greater than that which the Board has approved under the Franchise Agreement.

67. An additional implication of a competitive process is that the Board's jurisdiction to make a determination in the public interest to select the lowest cost alternative may be pre-empted since the municipality, by the time a municipal franchise application is made, will have already made the selection on its own criteria that may not take into account those parameters typically considered by the Board in awarding a franchise. Lower cost or more qualified distributors may have already been eliminated from the process or not intervene in the Board's process because the decision has already been made.

(b) *Global Subsidy*

68. As noted above, the Board has no jurisdiction to establish a global subsidy scheme.
69. In conjunction with a competitive process, EPCOR has proposed that the Board establish such a global subsidy. VECC, although not endorsing one particular approach, also put forward evidence describing a global subsidy in Canada's telecommunications industry.
70. EPCOR, through the testimony of Dr. Adonis Yatchew, has proposed that the Board establish and administer an expansion reserve fund which according to Dr. Yatchew, would be funded by a small volumetric levy on province-wide sales of natural gas to current customers.
71. In addition to lack of jurisdiction, the EPCOR proposal is one that is overly complex for the current expansion need and is unworkable without added regulatory rules and structure. Dr. Yatchew presented a proposal that was little more than a theoretical

construct that failed to consider the complex issues and mechanics that come with setting up, managing and operating such a fund.

72. The global subsidy proposal raises a number of unanswered questions, such as:
- Will all Ontario communities be eligible or only a select few - eligibility criteria is unknown.
 - As the subsidy will be determined on a prospective basis and will depend on the eligibility criteria, the forecast methodology for the amount of subsidy and the required amount in the reserve fund are unknown.
 - EPCOR proposes that the subsidy take the form of an aid to construct, which means that it is an upfront payment. However, it is unknown as to how the fund would accumulate sufficient reserves in advance of a project to adequately fund the desired aid.¹⁸
 - No insight was given as to the administration of the fund by the Board. In particular, what governance structure would the Board employ? Would the fund be independently managed and at what cost (Transcript, Vol. 4, p. 119)? Would the Board, as a corporate entity created by statute and agent of the Crown, have authority to levy, collect and disburse such a fund.
 - Mechanisms to recover the fund contribution from each of the gas distribution companies and then transfer those funds to the Board for purposes of administration in the fund remain unclear. Unlike in the RRRP regime where the IESO acts as a clearing agent, the Board would need to establish comparable rules as well as administrative roles and responsibilities in the OEB to review and settle accounts with the distribution companies as well as to administer the fund.
73. The foregoing are fundamental issues that must be resolved in order for a global subsidy approach to be considered. This would not occur without extensive consultation and proceedings by the Board to establish the appropriate resolution to the issues and a transparent development of program parameters that go well beyond the current generic proceeding (Mr. Hariton, Transcript Vol. 4, p. 119).
74. Furthermore, the complexity of a global subsidy regime must be evaluated in the appropriate context. As noted above, from Union's perspective, its own 29 community expansion projects would serve 18,000 new ratepayers, which is 1.2% of Union's current

¹⁸ Treating the subsidy as an aid to construct will have an effect on the PI such that fewer projects would be initiated.

customers and 0.5% of the ratepayers across the province. Union's proposal, as noted above, using existing and amended processes that are transparent and require no additional administration accomplish a more cost effective and time efficient result while providing the public interest benefit of expanding natural gas service to rural communities.

75. It was for the foregoing reasons that London Economics Inc., after assessing four alternative approaches for funding, indicated that Union's utility cross-subsidy approach is the most favorable when compared to the approaches of direct payment by natural gas expansion rate payers, jurisdiction-wide cross-subsidization or taxpayer funded subsidization (Union, Exhibit A, Tab 1, Schedule 1, p. 13-14).

G. RELATED ISSUES

(a) *Advancement Charge*

76. As a clarification to the economic assessment factors in EBO 188, Union proposes that, subject to conditions, the costs of upstream distribution system reinforcement should be included in the economic assessment of any new attachment. Where applicable, upstream distribution reinforcement cost assessment would occur in the form of either the direct capital cost of the minimum required level of reinforcement or an advancement charge or both.
77. The direct capital cost would be required at the time of connection in order to provide the capacity required for that connection.
78. Where adequate capacity is available in the upstream distribution system for a new connection, but future expected upstream distribution reinforcement timing will be accelerated to allow for other routine connections to the system, an Advancement Charge¹⁹ would be included in the Discounted Cash Flow ("DCF") to recognize the need for planned future capital reinforcement investment earlier than would otherwise be

¹⁹ The Advancement Charge is based on the difference between the NPV of the revenue requirement of a reinforcement project in a given year, and the NPV of the revenue requirement resulting from doing that same project in a later year.

expected. The application is fair and reasonable since the development of a major reinforcement can extend over a number of years and it would be unfair to tie up all existing capacity for the benefit of the customer triggering the reinforcement to the exclusion of other customers that may want to connect and would be subject to expansion costs that would otherwise not be incurred but for the reinforcement project.²⁰ In its application, Union proposes the Advancement Charge be restricted to situations where material new attachments would result in a need to accelerate future reinforcement to within three years following the year the attachment is put into service.

79. For example, generally, unutilized system capacity is made available on a first come, first served basis for any new load additions. Union attempts to ensure that capacity is available for reasonably forecasted general service customer attachments for a three year period, since the planning and execution cycle for a major reinforcement project can extend that long. Union does not want to be in a position where a small customer would be unable to connect because the system capacity has been fully exhausted and capacity will not become available for up to three years.
80. In addition to the above condition, Union proposes that the need for upstream reinforcement Advancement Charges be restricted to economic assessments where a new attachment or load addition consists of a load of 200 m³/hour or higher. Union proposes this level of load because it is material enough that it could have significant impact on future reinforcement timing, and roughly corresponds to the annual load which would qualify a customer for contract rates.
81. These two restrictions on upstream reinforcement Advancement Charges would strike an appropriate balance between a desire not to overburden community expansion projects with longer term reinforcement Advancement Charges when adequate capacity is currently available, and a need to ensure that adequate capacity remains available in the near term for routine general service customer attachments to the system (Exhibit A, Tab 1, p. 8-10).

²⁰ This approach was accepted in E.B.L.O 253 and E.B.L.O. 259.

82. Union has also made proposals under Issue 4, section (b) of its EB-2016-0004, Exhibit A, Tab 1 submission regarding the issue of 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. These proposals include Minimum Design Costs, Rate Based Revenues, Commercial/Industrial Revenue Time Period, and Customer Forecast Time Period. Union is of the view that these proposals continue to be appropriate issues for consideration of the Board.

(b) *Municipal Franchise Agreement Approval Process*

83. In Procedural Order No. 3, the Board asked parties to consider questions relating to the Municipal Franchise Agreement approval process. In Union's view, the Board should not review or change the existing form of franchise agreement or the corresponding approval process. Rather, the Board should re-affirm its expectation that the current model franchise agreement should continue to be adopted on a consistent basis across the province without significant deviation and re-assert that it is ultimately within the Board's determination as to whether a proposed franchise agreement will be acceptable in the public interest. This public interest determination enables the Board to consider aspects such as the proposed rate structure, the experience and capabilities of the franchisee and whether the proposed franchisee will be capable of meeting the minimum requirements for a gas distributor. As described in Exhibit S15.Union.Energy Probe.13, these minimum requirements can broadly be understood as relating to demonstrated operational capability, the ability to meet the core expectations that the Board has for existing gas utilities in Ontario, and demonstrated financial stability.

(c) *Loan and Grant Program*

84. With respect to the Province's pending loan and grant program, Union is of the view that the process for obtaining such funding is between the connecting Party and the government. Any funding obtained would become an input to the economic analysis of a project as it would, if provided as an aid-to-construction, reduce the capital costs of the project or, if in another form, reduce the annual revenue requirement. Under Union's proposed approach, Union's 29 Community Expansion Projects would be able to proceed

without provincial funding, thereby enabling the corresponding 33 communities to get access to gas service sooner.

H. CONCLUSION

Placed between the two ends of the spectrum of the status quo and the competition/global subsidy approaches, Union's approach provides a rational and principled basis for the expansion of gas services to unserved communities. Union's proposed approach uses established regulatory mechanisms, is within the Board's jurisdiction, and provides a fair and reasonable balance in a transparent and efficient manner so as to advance the principal policy objectives.

All of which is respectfully submitted this 20th day of June, 2016.

UNION GAS LIMITED

By its Counsel

Torys LLP



Charles Keizer



Crawford Smith