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BY EMAIL and RESS

June 22, 2016
Our File: EB20150363

Ontario Energy Board
2300 Yonge Street
27th Floor
Toronto, Ontario
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Attn: Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: EB-2015-0363 – Cap and Trade Regulatory Framework – SEC Comments

We are counsel to the School Energy Coalition ("SEC"). Pursuant to the Board's letter dated May 25, 2016, these are SEC's comments regarding the *Staff Discussion Paper on a Cap and Trade Regulatory Framework for Natural Gas Utilities* ("Staff Report").

Overview

The Ontario Government's Cap and Trade Program is a far-reaching program that will require dramatic reductions in Greenhouse Gas ("GHG") emissions over the next 35 years, with a significant portion of that coming from natural gas. This will lead to significant changes in the natural gas industry in Ontario. The Board will play a central role in facilitating this change, and it begins with properly aligning the objectives of Cap and Trade in the setting of natural gas rates. Schools are and have been strong supporters of, and early participants in, initiatives to fight climate change.

Under the *Climate Change Mitigation and Low Carbon-Economy Act* (the "*Act*"), and the Cap and Trade Regulation (O/Reg 144/16) (the "Regulation"), natural gas utilities will have the compliance obligations not just for their own facilities related emissions, but also for their customers' natural gas related emissions for all those but Large Final Emitters and Voluntary Participants. That is, natural gas utilities are required to meet the compliance obligations for their customer's use of natural gas, in addition to their own use.

While customers are not directly responsible for meeting their compliance obligations, they will still be paying for that compliance, as those costs will be included in rates. Like all other rate-setting, the Board's mandate is to ensure the utilities' activities are prudent, and lead to just and reasonable rates.

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SEC notes that the Staff Report focuses only on the utility Compliance Plans under Cap and Trade, and related issues. It does not take into account the remainder of the Government's Climate Change Action Plan, released on June 7th 2016, which provides details of planned government actions, including significant spending, to reduce GHG emissions in Ontario.[1] SEC accepts that it was appropriate for the Staff Report to keep its focus narrow, since there are a number of technical and policy requirements that are specific to the Cap and Trade component of the Action Plan.

The Climate Change Action Plan implicitly raises the possible of material demand destruction due to a shift away from fossil fuel use for some energy functions. This will have a significant impact on the overall natural gas industry in the province, including Cap and Trade compliance.

SEC believes that the scope of the Board's review of the utilities' plans to deal with climate change should not be limited to the Compliance Plans under the regulation. While that is a step in the process, SEC submits that the larger strategic issue of the changes to the natural gas industry should be the subject of utility plans, and Board oversight, on an urgent basis.

Specific Submissions

SEC is in *general* agreement with most of the Staff Report on what should be included in a utility compliance plan, as well as how the cost will be recovered from ratepayers. With that said, SEC does have some important and specific concerns about a few elements of the Staff Report, discussed below:

2017 Plan Needs To Be Made In the Context Of Full Compliance Period. SEC agrees that a three-year Compliance Plan to align with the entire compliance periods are appropriate, but that since the first compliance period is four years, the utilities should submit a one-year plan for 2017, and then afterwards file a three year plan. Since Cap and Trade is new, and there will be no linked market until 2018, a one year initial Compliance Plan makes sense. With that said, a one-year plan in isolation will be of little use for the Board. The Board should ensure that the utilities explain, in their first one-year Compliance Plan, how their strategy in the 2017 will relate to the rest of the compliance period. While they may not be held to it like they would for a regular three-year Compliance Plan, it will give the proper context needed to judge the reasonableness of the 2017 Compliance Plan.

Marginal Abatement Cost Curve. Staff recommends that there should be one general Marginal Abatement Cost Curve ("MACC") that would either come to be created by the utilities together, or from Staff. The utilities on their own may choose to develop a company-specific MACC to inform the development of their individual Compliance Plans. SEC believes that there may be some limited value in a generic MACC that outlines general, non-utility-specific compliance and abatement activities available in the market. The purpose of it should only be as a way to reasonableness of the utility-specific MACCs insofar as they themselves influence their individual Compliance Plans. Because of that it makes sense for the general MACC to be developed by Board Staff. The utility specific MACCs will be very important, and should not just be optional but required, especially if the Board is expecting utilities to come forward with abatement activities which by their very nature will be unique to its customer mix.

Not Just Enbridge and Union. While the province is currently dominated by two utilities (Enbridge and Union Gas), any Cap and Trade framework needs to be applicable to all distributors regulated

[1] Government of Ontario, *Climate Action Plan*
<http://www.applications.ene.gov.on.ca/ccap/products/CCAP_ENGLISH.pdf>

by the Board. While there will be very different considerations for a utility like NRG, and potentially EPCOR[2], they will still be required to comply with the Cap and Trade program.

Abatement Programs. The Staff Report seems to indicate the expectation that the Compliance Plans will include DSM-type abatement programs. The Staff Report says that these costs will need to be incremental to the 2015-2020 multi-year DSM programs.[3] It is not clear from the Staff Report with what lens OEB Staff believes the Board should review these abatement programs. Will it be the same way it evaluates DSM programs consistent with the Board's DSM Framework[4] using the same cost-effectiveness and shareholder incentive system, or will it be considered as a wholly separate system?

SEC believes that DSM-type programs directed at abatement should not be treated in the same way as standard utility DSM programs. First, the programs need to be compared to GHG compliance alternatives, not to TRC or similar tests. While the latter may be relevant to identifying the other benefits of the programs, the incremental spending is justified by its ability to deliver GHG reductions at a lower cost. Second, there is no reason to have a shareholder incentive for these programs. Just as there is no incentive for purchasing allowances, or reducing facilities emissions, so there should be no incentive for incremental DSM that meets a statutory obligation.

Furthermore, the Board must also ensure that any framework requires that any proposed abatement programs are aligned with the recently released Climate Change Action Plan. The Board should ensure that the utilities are not paying for abatement programs which are working at either cross-purposes or in competition with programs being funded from the Climate Action Plan, for which they are also paying.

Risk Management Activates. The Staff Report supports the use of risk management activities, such as hedging and trading of allowances and other compliance instruments in the secondary and tertiary markets. SEC understands some stakeholders oppose this for similar reasons that caused the Board to determine previously that such activities would not be allowed with regards to a utilities gas supply portfolio.

SEC accepts that the conclusions in the Staff Report that this situation is different. Moreover, in the gas supply context, ratepayers always have the option of becoming a direct purchase customer to take advantage of these risk management practices if they so choose. Here, there is no such option except for a Voluntary Participants, who while not Large Final Emitters, are still large very emitters.

At the same time, there is simply not information available at this time for SEC to make a final recommendation on this issue at this time. Board should allow utilities to come forward with risk management plans in their Compliance Plans. At that the point the Board will have more information to make a final determination if allowing these activities is appropriate, and if so, to what degree.

Customer-Related Obligations Should Be A Separate Line Item on the Bill. The Staff Report recommends that the compliance costs should not be a separate line on a customer' SEC disagrees and submits the customer compliance-related obligation costs should be a separate line item.

The intent of the Cap and Trade program is to send price signals to those who emit GHG emissions, in this case, natural gas customers who when consuming natural gas release GHG emissions into

[2] EPCOR Inc. has filed a franchise agreement with three municipalities it seeks to bring natural gas service to (EB-2016-0137/138/139)
[3] *Staff Discussion Paper on a Cap and Trade Regulatory Framework for Natural Gas Utilities* ["Staff Report"], p.21, footnote 4
[4] *Report of the Board: Demand Side Management Framework for Natural Gas Distributors* (2015-2020), December 22 2014

the atmosphere. Without knowing the price they are paying for compliance (the cost of GHG emissions), they are unable to make informed decisions to reduce their consumption. Customers need to understand, through bill presentment, that these added costs are more than just the cost of the utility providing a service to them. These specific costs are being recovered on their behalf to pay for their share of GHG emission reductions.

Customers should see directly how much it is costing them to emit GHGs. They should be able to connect that cost with their use, so that they can decide to reduce their emissions, and therefore reduce that cost. It is not only Large Final Emitters that need a price single. The individual homeowner needs that signal as well.

SEC recognizes that for your average customer, there may be some confusion, insofar that they believe the customer-related obligations represent all Cap and Trade or GHG related costs they are being required to pay. This is not the case, as there are not just Cap and Trade costs (facilities related and administration costs) that would not be included in this line-item, but also other GHG related costs (DSM, and upstream GHG costs) that are embedded in different parts of the bill. SEC agrees that some should be excluded (they are not directly costs of the customer's emissions from its use, and they are thus not avoidable by customer decisions in most cases), but the others probably should be included in the the separate line item (they are directly driven by the customer's consumption). The unfortunate truth is that the latter cannot easily be segregated, and included in this line.

The answer to this problem is not simply to include no information on a separate line item, but rather to explain to customers by way of bill insert or other messaging what is being included and what isn't. It may even be possible to include an estimate of the additional per cubic meter costs for DSM, upstream emissions, and a facility-related obligations that related to transportation infrastructure (i.e. emissions from compressor), in that messaging, without having to do a formal calculation for inclusion in the line item.

Confidential Material. Board Staff recommends that two types of information (auction and market sensitive information) not just be dealt with on a confidential basis, but also not be disclosed to any party in the proceeding. SEC disagrees with the Staff Report on this issue.

i. **Auction Confidential Information.** SEC accepts that section 32(6) of the *Act* and the Cap and Trade Regulation do not allow certain information to be provided to anyone but the Board. The information is any disclosure about "whether or not a person is participating in an auction".[5] SEC submits that allowing only Staff and the Board panel to review this information does not allow for proper scrutiny by ratepayers to determine the prudence of the expenditures. The Staff Report recommends that Staff review the information and provide a non-confidential report as to the reasonableness and prudence that is the outcome of this information. SEC submits this is wholly inappropriate. While Staff may opine on its view of the reasonableness and prudence, it is not their job to make that determination. It is the Board's role to make that determination.

   SEC submits the way to ensure proper scrutiny of any costs that turn on this auction information is that they should only be approved on an interim basis until after the auction has been completed. The restrictions are for future-looking information about participating in a specific auction. Once the auction is over there are no restrictions. The Staff Report envisions that Cap and Trade costs will be

[5] *Climate Change Mitigation and Low-carbon Economy Act*, 32(6),(7)

trued-up on an annual basis.[6] The Board can have, at that time, an after-the fact prudence review which would allow all parties to review the necessary information without being in breach of the *Act*. Without such a review, the transparency of the process, and the public's trust in it, may be harmed.

ii. ***Market Sensitive Information.*** The Staff Report indicates that some information which will need to be provided in a utility's Compliance Plan could be market sensitive and should not just be treated confidentiality pursuant to the *Practice Direction on Confidential Filings* ("*Practice Direction*"), but should kept secret from everyone except the Board panel and Staff. The Staff Report's justification is that, if disclosed, there will be market harm and such public disclosure may lead to certain actions that are prohibited under the *Act*.

SEC disagrees with this approach. Unlike the prohibition on disclosure regarding information about auction participation, there is no such statutory prohibition on disclosure of this information. What there are is specific prohibitions on trading on non-public information and so there is a benefit on restricting its disclosure. This is not a new issue for the Board to consider. The same or similar prohibitions on the inappropriate use of non-public information exist currently under the *Ontario Securities Act*. The Board's *Practice Direction* specifically mentions confidential treatment of "financial information that has not been publicly disclosed, and that Ontario securities law therefore requires be treated as confidential." [7] This Board has on many different occasions granted confidentiality status to non-public information that may affect public markets. Confidentiality status is often granted to certain future-looking financial information from utilities that access the public markets (Toronto Hydro, Hydro One, OPG etc.). The Board should not treat this information any different. To do so would be to diminish significantly the ability of parties to scrutinize this important information, and to determine the reasonableness of the Compliance Plans. This is especially important considering the Staff Report's position that the utilities should be allowed to be involved in risk management activities such as trading and hedging. Ratepayers will not be able to evaluate the reasonableness of these strategies and activities without access to this information.

Broad Scope Consultation Needed

As discussed at the beginning, the *Climate Change and Low Carbon Economy Act* is going to require significant changes to how natural gas utilities operate over the next 20 years. Enbridge's own consultant ICF, expects residential volumes to decline by 40% and industrial volumes 20-30% by 2030.[8] The Staff Report discusses only briefly the longer-term investments, such as new technologies and new infrastructure[9], as well as the treatment of new business [10]activities. These two issues are likely to be very significant over the next decade, as the utilities will be required to shift away from a business supplying conventional natural gas, to a new business that is potentially very different.

SEC believes these long-term strategic questions should be dealt with in a broader consultation, to be held on an urgent basis. This will allow ratepayers, other stakeholders, the utilities, and the regulator to consider the real long-term issues that will face the industry as we move to a carbon free economy.

[6] Staff Report, p.34
[7] *Practice Direction On Confidential Filings*, April 24, 2014, Appendix B, p.19
[8] Enbridge presentation to the 2015 Natural Gas Market Review (EB-2015-0237), slide 14
[9] Staff Report, p.24
[10] Staff Report, p.49

All of which is respectfully submitted.

Yours very truly,
Jay Shepherd P.C.

Original signed by

Mark Rubenstein

cc: Wayne McNally, SEC (by email)
Interested Parties (by email)