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June 22, 2016

VIA E-MAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge St.
Toronto, ON
M4P 1E4

Dear Ms. Walli:

**Re: EB-2015-0363 – Cap and Trade Regulatory Framework for Natural Gas Utilities
Comments of the Vulnerable Energy Consumers Coalition (VECC)**

Please find enclosed the Comments of the Vulnerable Energy Consumers Coalition (VECC) with respect to the above-noted proceeding.

Yours truly,

A handwritten signature in black ink, appearing to be 'Michael Janigan', written in a cursive style.

Michael Janigan
Counsel for VECC

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Vulnerable Energy Consumers Coalition

EB-2015-0363 - Consultation to Develop a Regulatory Framework for Natural Gas Distributors' Cap and Trade Compliance Plans

Submission on the Board Staff Discussion Paper on a Cap and Trade Regulatory Framework for Natural Gas Utilities

Executive Summary

One of Board's Objectives Statutory Objectives is "to promote energy conservation and energy efficiency in accordance with the policies of the Government of Ontario, including having regard to the consumer's economic circumstances". Vulnerable Energy Consumers Coalition ("VECC") consists of the Federation of Metro Tenants Association (FMTA) and the Ontario Coalition of Senior Citizens Organizations ("OCSCO"). FMTA is a non-profit corporation composed of over ninety-two affiliated tenants associations, individual tenants, housing organizations, and members of non-profit housing co-ops. OCSCO is a coalition of over 160 senior groups as well as individual members across Ontario. OCSCO represents the concerns of over 500,000 senior citizens through its group and individual members. The majority of consumers that VECC represents have very limited economic resources and are constrained in their ability to mitigate increased costs that will be downloaded to them by Cap and Trade. VECC urges the Board to adopt a framework that will minimize the impact on vulnerable apartment tenants and senior citizens who are unable to mitigate their use of natural gas. The framework should also stress transparency, effective monitoring, and simplicity of approach. The Board should also ensure that the Cap and Trade framework does not become a profit making enterprise for gas distributors where the equity returns to utility shareholders are extracted from low income tenants and seniors on fixed income.

Background

On May 25, 2016 the OEB issued a letter to all participants in EB-2015-0363 and released a discussion paper by Staff on a Cap and Trade Regulatory Framework for the Natural Gas Utilities. The letter invited stakeholders to comment on all of the issues, options and proposals set out in the discussion paper. VECC has reviewed the discussion paper and has provided its

comments in this submission. The comments are sequenced to correspond with the organization of the discussion paper.

Guiding Principles and Framework

OEB staff's discussion paper proposed that the framework should be guided by OEB's statutory objectives. Let's look at the OEB's statutory objectives as set out in the OEB Act.

Board objectives, gas

The Board, in carrying out its responsibilities under this or any other Act in relation to gas, shall be guided by the following objectives:

- 1. To facilitate competition in the sale of gas to users.*
- 2. To protect the interests of consumers with respect to prices and the reliability and quality of gas service.*
- 3. To facilitate rational expansion of transmission and distribution systems.*
- 4. To facilitate rational development and safe operation of gas storage.*
- 5. To promote energy conservation and energy efficiency in accordance with the policies of the Government of Ontario, including having regard to the consumer's economic circumstances.*
 - 5.1 To facilitate the maintenance of a financially viable gas industry for the transmission, distribution and storage of gas.*
- 6. To promote communication within the gas industry and the education of consumers.*

The relevant objectives are 2, 5, and 6.

In objective 2, the Board shall be guided "to protect the interests of consumers with respect to price...". VECC believes that the Board the meaning of "protect the interest" in the context of Cap and Trade refers to ensuring that consumers are not charged any profit mark-up on Cap and Trade and that administrative costs be minimized, transparent and audited.

In objective 5, the Board shall be guided "To promote energy conservation and energy efficiency in accordance with the policies of the Government of Ontario, including having regard to the

consumer's economic circumstances." The objective of Cap and Trade is to reduce the use of natural gas by increasing the cost charged to its consumers to provide the consumers with the incentive to cut their use of natural gas. The vast majority of the consumers represented by VECC will have difficulty reducing their use of natural gas. In most apartments, the tenants do not have direct control over the central heating boiler in the basement. The additional costs of Cap and Trade will be passed through by landlords to tenants. In seniors' retirement homes and assisted living establishments, the residents have no control over heating. Additional costs brought on by Cap and Trade may simply be passed through to the residents by the operators. Seniors living in their own homes frequently do not have the financial resources or the revenue horizon to invest in more efficient appliances or in additional home insulation. Cap and Trade will therefore be an immediate additional cost to them that they will not be able to mitigate. VECC urges the Board to adopt a framework that will minimize the impact on vulnerable apartment tenants and senior citizens who are unable to mitigate their use of natural gas.

In objective 6, the Board shall be guided "to promote communication within the gas industry and the education of consumers." The primary means of communication with consumers is the customer's bill. The bill should clearly communicate the cost of Cap and Trade that the customer is being asked to pay.

Board Staff then presents six guiding principles for the framework: cost-effectiveness, rate predictability, cost recovery, transparency, flexibility, and continuous improvement.

Cost-effectiveness: *Compliance Plans are optimized for economic efficiency and risk management. VECC supports this principle.* As VECC understands it, utilities would meet their emission targets by purchasing allowances or by aggregating the conservation measures of their customers. The Board should ensure that the most effective and efficient combination of these alternatives is used in order to minimize the impact on consumers. Regarding risk management, it is not clear at this time that risk management ought to be used by utilities for Cap and Trade. As the Board is aware, utilities past experience in gas cost risk management resulted in large losses which had to be absorbed by utility customers. The Board should think very carefully before it allows large scale risk management activities.

Rate predictability: *consumers should have just and reasonable, and predictable rates regarding the impact of the utilities' cap and trade activities.* VECC supports this principle but has some concerns. It is not clear how the will decide if rates charged to consumers are just and

reasonable. Since rates will be based on a forecast of the price of carbon that will be adjusted on an annual basis, actual prices are likely to be different. That would probably need to be managed through a variance account mechanism. The clearance of such a variance account is likely to produce an element of rate unpredictability.

Cost Recovery: prudently incurred costs related to cap and trade would be recoverable as a cost pass-through (similar to natural gas supply procurement). VECC supports this principle.

Transparency: investment/buying strategies and optimization processes are transparent and well documented to facilitate the OEB's assessment of the plans and costs, while ensuring market integrity. VECC supports this principle but believes that it should be extended to the presentation of all charges on a customer's bill.

Flexibility: plans are flexible and can adapt to changing market conditions and utility-specific characteristics; potential for framework to evolve as market matures and experience is gained. VECC supports this principle.

Continuous Improvement: plans demonstrate continuous improvement of processes and practices, including the use of existing systems. VECC does not unreservedly support this principle because it is vague and open to abuse to justify continuous increases in spending the costs of which are passed to ratepayers. Improvement should mean being able to do more with fewer resources.

4 Compliance Plans

Under the regulatory process outlined by Board Staff each gas distributor would file its Cap and Trade Compliance Plan for OEB approval. The OEB would review the plans to determine whether to approve the associated cap and trade costs for recovery from ratepayers. Because these plans will have a large cost impact on ratepayers, VECC urges the Board to adopt a regulatory process that will allow for full and complete public scrutiny of the plans.

4.1 Issues and Options

Board Staff proposed a list of Issues and Options.

1. *Level of OEB Guidance*
2. *Duration of Compliance Plans*

3. Forecasting

4. Assessment of Compliance Plans

5. Treatment of Longer-term Investments

To this list VECC proposes the following issue be added:

6. Public Scrutiny

According to a well known saying: “if you’re not at the table, you’re probably on the menu”. If ratepayers are not at the table to see what the utilities and Board staff are planning it is probable that ratepayers will be “on the menu”, that is, ever increasing costs will be downloaded on them. In this instance, the Board is implementing government policy and cannot be relied to protect the interests of ratepayers. It is a given that utilities will protect the interests of their shareholders.

4.1.1 Regulatory Approach to Compliance Plans

Staff is proposing that the OEB follow something they call a “light-handed approach” in its assessment and approval of compliance plans for cost recovery from ratepayers. VECC is mindful that a light-handed approach has sometimes produced what one American regulator, Peter Bradford, has called a “light-fingered approach “ by regulated utilities. Full public scrutiny must be allowed. Cap and Trade Compliance Plans are a new concept that needs to be fully explored to ensure that ratepayers are protected from unwarranted costs and gaming of the system by utilities. If Compliance Plans include investments, VECC urges the Board to require that each investment be supported by rigorous business case that is filed for review and approval by the Board in an open regulatory proceeding. Considering the potentially high costs and long term implications of such investments, ratepayers should have a right to ask interrogatories and to cross examine utility witnesses.

Board Staff proposes that the OEB would set out the basic parameters, including the approach it would take to assess the utility’s plans and information that it would expect to see in a plan. VECC believes that parameters that would be used to assess utility’s plans are a key element that would ensure the legitimacy of the entire OEB Cap and Trade process. If the assessment parameters are unduly complicated and only understood by the experts, the legitimacy of the

OEB Cap and Trade process will be put in question. The assessment parameters must be simple and rigorous so that they can be explained to the utility ratepayers. They must not become like the arcane assessment parameters that is being used for the assessment of DSM plans that are incomprehensible to ordinary ratepayers. VECC urges the Board to seek input from the public in the development of assessment parameters.

Board Staff proposes that utilities be responsible for deciding on the exact makeup of their Compliance Plan portfolios but that these be subject to OEB approval and that the OEB would assess the plans to ensure cost-effectiveness and reasonableness for the purpose of cost recovery from ratepayers. Considering that ratepayers will be paying for this, they must be involved in all steps of the process. As it appears now, in the process outlined by Board Staff there are no incentives to control costs since all costs are recoverable from ratepayers. It is therefore essential that ratepayers be consulted at all steps. This is particularly essential since as Board Staff says *“the market will be nascent and there could be considerable market uncertainty”*.

4.1.2 Duration of Compliance Plans

Board Staff considered two alternatives: annual plan and a multi-year plan that matches the compliance periods in the Cap and Trade Regulation. Their proposal is that there be a one year plan for 2017 followed by multi-year plans for subsequent years. One of the reasons for this that Board Staff put forward is that in the first year, Ontario cap and trade market will not be linked to other markets in the Western Climate Initiative. Therefore it is likely that when the Ontario market is linked to other markets in 2018 the conditions will be so different that a compliance plan that was effective in 2017 is no longer effective. To allow the OEB to properly assess the effectiveness of compliance plans under linked market conditions VECC believes that each utility should file two one year plans, one for 2017 and one for 2018. These could be followed by multi-year plans if the review of 2017 and 2018 actual results demonstrates that the utilities have gained sufficient experience to warrant it.

4.1.3 Forecasting

Compliance plans will be based on three key forecasts: load forecasts, GHG emissions forecasts, and carbon price forecasts. As explained above, VECC believes utilities should file two one year forecasts, one for 2017, the year with stand alone Ontario market 2017, and one

for 2018 when the Ontario market is linked to other jurisdictions. After these forecasts are compared to actual results and utilities' forecasting accuracy is evaluated should the OEB consider moving to multi-year forecasts. Utilities have no experience in forecasting GHG emissions or carbon prices. Moving prematurely to longer term forecasts could lead to large variances. For carbon price forecasts, Board Staff proposes that the ICE forecast be used. Considering the importance and the cost impact the carbon price forecast, VECC urges the OEB to conduct a full and unbiased review of alternatives before making its decision.

4.1.4 Compliance Plan Assessment

According to the process outlined by Board Staff utilities would file their Compliance Plans with the OEB for approval and recovery of costs from ratepayers. The plans will then be assessed according to certain assessment criteria and either approved or rejected.

4.1.4.1 Objectives of Compliance Plan Assessment

Board Staff proposes that compliance plans be assessed to see if they meet the objectives of being optimized, integrated and adaptable. As described by Board Staff these three adjectives are not objectives and are unlikely to provide the basis for a meaningful assessment.

According to Board Staff, "optimized" means that a Compliance Plan is *"characterized by strategic decision-making and risk management, resulting in a portfolio of compliance options that is cost-effective"*. It is not clear how the Board would be able to determine in a compliance plan is optimized or not. Guidance provided in section 4.1.4.2 of the Board Staff paper is not of much help.

"Integrated" is defined by Board Staff as *"procurement and investments in GHG abatement activities (that) should be approached 'holistically' to extract maximum value from long-term commitments that integrate multiple benefits as this should be more cost-effective than a narrow, short-term planning approach"*. This vague definition would be of no help in assessment of a Compliance Plan. The third objective, "adaptable" is defined as *"flexible enough to adapt to changes in market conditions and changes in load, as well as other sources of risk."* It is not clear how one would assess this.

4.1.4.2 Optimized Portfolio

Staff expects that the utility will demonstrate optimization by providing certain information. It is not clear if the information will include numerical information. For example, if a utility specific Marginal Abatement Cost Curve (“MACC”) is provided, it should not only be provided in pictorial form but should include all of the numerical information used in its derivation. Similarly, Options Analysis should explain how it was performed showing all calculations. Staff suggests that the timeframe for MACC be 10 years starting in 2018. VECC believes that more time is needed to develop MACC and that the 10 year period should start in 2019 at the earliest. MACC should also be reviewed and updated on an annual basis.

4.1.4.3 Risk Management

Board Staff proposes that utilities participate in cap and trade risk management activities despite the fact that the OEB specifically prohibited gas supply risk management activities in its EB-2007-0606 decision. The Board reached that decision after utilities incurred substantial losses as a result of their risk management activities. There is no indication that cap and trade risk management would not result in large losses. In fact there is a high probability that it would result in losses considering recent collapse of the carbon market in Europe and the weakness of the carbon market in California. VECC urges the OEB to either prohibit risk management activities or place very strict limits on the size and scope of such activities and set maximum amount of loss that can be recovered from ratepayers. Board Staff suggests that any concerns could be addressed by having “robust governance systems in place”. Board Staff should recall that robust governance systems of the utilities did not protect them from sharp declines in the commodity markets in the past.

4.1.5 Treatment of longer term investments

From ratepayer perspective it must be clear at the outset if longer-term investments that utilities would be proposing are investments in utility owned assets on utilities’ premises or are they multi-year programs of investments on customer owned assets located on customers’ premises. For rate making purposes, investments in customer owned assets cannot form part of rate base. Only utility owned rate base assets are subject to equity return.

5 Cost Recovery

Board Staff identify three types of costs that would be subject to cost recovery: facility-related obligations for facilities owned or operated by the utility, customer-related obligations for natural gas-fired generators and residential, commercial and industrial customers who are not Large Final Emitters or voluntary participants, and administrative costs to meet its compliance obligations.

For the purpose of cost recovery any spending on GHG compliance must be clearly identified as either Capital or OM&A. Spending on facility-related obligations for facilities operated by the utility can be either treated as capital or OM&A depending on the type of expenditures. Spending on customer-related obligations can only be treated as OM&A.