

# Elson Advocacy

January 15, 2020

**BY COURIER (2 COPIES) AND RESS**

**Ms. Christine Long**

Board Secretary  
Ontario Energy Board  
2300 Yonge Street, Suite 2700, P.O. Box 2319  
Toronto, Ontario M4P 1E4

Dear Ms. Long:

**Re: EB-2019-0255 - Potential Projects to Expand Access to Natural Gas Distribution**

We are writing on behalf of Environmental Defence to provide comments on the draft Guidelines for Potential Projects to Expand Access to Natural Gas Distribution. Environmental Defence provides these comments as a leading environmental organization with deep knowledge and expertise in the financial costs and risks associated with climate change to energy consumers. We believe this knowledge and perspective could assist the Board in improving the Draft Guidelines to better protect the interests of gas consumers in Ontario.

As you might expect, Environmental Defence does not support subsidies to expand fossil fuel infrastructure. However, we understand that this broader question is outside of the scope of this consultation. Our comments are limited to proposed changes to better protect the interests of gas consumers, with a particular focus on protecting them from the costs and risks associated with climate change.

As detailed below, we ask the Board to update the Guidelines to fully hold proponents to their financial forecasts, require a sensitivity analysis regarding financial risks associated with climate change, and target energy efficiency programs to the potential new customers to ensure that they capitalize on the opportunity to purchase the most efficient equipment possible.

## **Hold Proponents to Financial Forecasts**

Environmental Defence believes proponents should be held to their financial forecasts and bear the risk that those forecasts are not met. Gas expansion projects are financially risky because the forecast revenue depends on customers spending significant sums to convert their homes or businesses to natural gas. If fewer customers convert than forecast, the project will miss financial targets. Without mechanisms to protect against this, the cost and risk is unfairly borne by existing gas customers. They could be on the hook for many millions of dollars if the forecast number of conversions do not materialize.

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This financial risk is much higher today than it was in the past. Climate change is causing accelerating changes in energy use patterns. Regulation and market forces are increasing the attractiveness of alternatives to fossil fuels. In five years, natural gas may not be the preferred option for customers in the relevant communities. In ten years, that is even more likely to be the case. Even more so in 20 years or longer.

For example, increased carbon pricing could cause consumers to convert to efficient electric heat pumps instead of natural gas furnaces.<sup>1</sup> This could also happen as the result of any number of other factors, such as subsidies for low-carbon alternatives, increased economies of scale for low-carbon alternatives, technological advancements, increased accounting of fugitive emissions associated with natural gas fracking and transmission, and so on. These eventualities must be considered and accounted for. If they are ignored, revenue forecasts will be missed and existing natural gas customers will end up on the hook.

The financial risks associated with continued investments in fossil fuels are widely acknowledged by financial leaders. For example, Mark Carney recently warned that global warming could render the assets of many financial companies worthless because they have been too slow to cut investment in fossil fuels.<sup>2</sup>

The only way to protect natural gas consumers is to hold proponents to their forecasts. This will ensure that proponents consider and account for these risks and build in an appropriate buffer.

Board Staff has proposed the following solution:

*Proponents would bear the risk for the 10-year period (or longer if proposed) if the customers they forecast do not attach to the system and/or actual project costs (capital and OM&A) are higher than expected.*<sup>3</sup>

This is very positive. However, we believe more is needed. We believe the proponents should be held to their forecasts full stop, without a 10-year limitation. This is important because:

1. **Government Direction:** The government directed the Board to ensure that proponents “be held to the project cost, timelines and volumes forecasts as set out in their project proposal.”<sup>4</sup> This does not contemplate forgiveness for missed forecasts after 10 years.

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<sup>1</sup> Canada’s Ecofiscal Commission, *Bridging the Gap: Real Options for Meeting Canada’s 2030 GHG Target*, November 2019, <https://ecofiscal.ca/wp-content/uploads/2019/11/Ecofiscal-Commission-Bridging-the-Gap-November-27-2019-FINAL.pdf>.

<sup>2</sup> Financial Post, *Global warming could render the assets of many financial companies worthless, Mark Carney warns*, December 30, 2019, <https://business.financialpost.com/news/fp-street/boes-carney-says-finance-must-act-faster-on-climate-change>.

<sup>3</sup> Letter from the Ontario Energy Board, December 19, 2019, p. 3

<sup>4</sup> Section 53 Directive from the Minister of Energy to the Ontario Energy Board, December 12, 2019, p. 2.

2. **\$130 Million Cap:** The government has capped the subsidy from existing customers at \$130 million. This can only be achieved by insulating existing customers from the risk of covering deficits beyond the first 10 years.
3. **Risks Increase Over Time:** The risk of lower customer conversions increases with time as the need to reduce carbon emissions increases. It is important to insulate existing customers from those greater future risks.

To protect existing customers, proponents must be held to their financial forecasts and bear the risk that those forecasts are not met initially and beyond the first 10 years.

### **Risk and Sensitivity Analysis**

Proponents should also be required to provide a sensitivity analysis with respect to their customer attachment forecast (s. 3.2 & 3.3) and profitability index (s. 7.1). This sensitivity analysis should address a scenario where government regulation and market forces significantly increase the attractiveness of low-carbon alternatives such as heat pumps vis-à-vis natural gas conversions.

To model this, the scenario could assume a carbon price that would achieve Canada's 2030 greenhouse gas reduction targets.<sup>5</sup> It is highly plausible that a carbon price will be implemented along those lines in the next 10 years. However, this scenario would not assume that this would, should, or could occur. Instead, the carbon price assumption would be a proxy for a scenario involving a combination of future climate regulation or market changes in support of low-carbon technologies (e.g. heat pumps), such as those possibilities mentioned above. The benefit of this approach is that it would only require proponents to examine one easy-to-understand alternative scenario.

A sensitivity analysis is critical for the Board in considering potential projects. The financial risks associated with fossil fuels may be higher for some projects than others. For example, some projects may be driven in large part by industrial consumers converting to natural gas from high-carbon fuels. These projects would be less sensitive to climate risks in comparison to those relying on conversions from low-carbon residential electric space and water heating. It is important for the Board to know which projects pose greater and lesser risks.

### **Targeted Energy Efficiency Programs**

Proponents should be required to propose targeted energy efficiency programs for the expansion areas. Strong energy efficiency program proposals should be an important factor in deciding which projects are selected.

Community expansion projects will create major opportunities to advance energy efficiency because new customers will be purchasing new equipment. Those potential customers should be

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<sup>5</sup> Canada's Ecofiscal Commission, *Bridging the Gap: Real Options for Meeting Canada's 2030 GHG Target*, November 2019, <https://ecofiscal.ca/wp-content/uploads/2019/11/Ecofiscal-Commission-Bridging-the-Gap-November-27-2019-FINAL.pdf>.

targeted with outreach efforts and incentives to ensure that they purchase the most efficient equipment.

Purchasing inefficient equipment represents a major lost opportunity that locks in higher-than-necessary costs for customers and the gas system as a whole. Equipment efficiency upgrades are typically only cost effective as an incremental cost when the equipment must be replaced at the end of its life. If customers are not incentivized to purchase the most efficient furnaces and water heaters, it will likely be more than a decade before doing so would be cost-effective. It is critical that these customers be targeted now, while the opportunities still exist.

Community expansion projects also create other energy efficiency opportunities because the proponents will be working directly with customers and have their attention. This will create a window to advertise home retrofit and other energy efficiency measures.

### **Conclusion**

As Mark Carney warns, climate change represents a major financial risk. That risk is particularly high for energy consumers investing in fossil fuel infrastructure. As detailed above, the Guidelines should be updated to allow the Board to better mitigate these risks.

Yours truly,

A handwritten signature in blue ink, appearing to read 'K. Elson', written over a horizontal line.

Kent Elson