

Ontario Energy Board



G-2010-0030

Guidelines:

**Regulatory and Accounting Treatments for
Natural Gas Utility-Owned Qualifying
Facilities or Assets**

February 25, 2010

1. Purpose

This document sets out a regulatory framework for the regulatory and accounting requirements for natural gas utilities, namely Enbridge Gas Distribution Inc. (“Enbridge”) and Union Gas Limited (“Union”), in relation to the ownership and operation of renewable energy generation facilities, combined power and thermal (heat) energy generation facilities, energy storage facilities and assets in relation to energy conservation (collectively referred to below as “qualifying facilities or assets”).

This document contains the Board’s guidance to natural gas utilities in relation to the Minister’s Directive issued to the Board and approved by Order in Council No. 1540/2009 dated September 8, 2009, which effectively authorized Enbridge and Union to own and operate qualifying facilities or assets. In terms of generation and energy storage facilities, this authorization mirrors the amendment to the *Ontario Energy Board Act, 1998* (“*OEB Act*”) that allows electricity distributors to own and operate the same qualifying facilities. The amendment to the *OEB Act* came into effect when the relevant provisions of the *Green Energy and Green Economy Act, 2009* came into force on September 9, 2009.

The purpose of this document is to describe the ownership scenarios that are potentially applicable in relation to assets and activities associated with qualifying facilities or assets that are not rate-regulated (i.e., whose costs are not included in rate base),¹ and to set out the regulatory and accounting requirements applicable to each scenario.

2. Legal Framework

2.1. The Undertakings

The activities of Enbridge and Union are governed in part by certain undertakings given to the Lieutenant Governor in Council.² Under section 2.1 of these undertakings, Enbridge and Union cannot, except through an affiliate, carry on

¹ In its December 22, 2009 Decision on a Preliminary Motion (EB-2009-0172), the Board declined to allow the costs of Enbridge’s “Green Energy Initiatives” to be included in rate base.

² The undertakings that are currently in effect were approved by Order in Council 2865/98 dated December 9, 1998.

any business activity other than the transmission, distribution or storage of gas without the prior approval of the Board.

2.2. Minister's September 2009 Directive

Order in Council No. 1540/2009 dated September 8, 2009 approved a Minister's Directive to the Board that effectively permits Enbridge and Union to own and operate qualifying facilities or assets.

The Minister's Directive, a copy of which is reproduced in Appendix A together with Order in Council No. 1540/2009, specified among other things, the following:

Pursuant to section 27.1 of the Ontario Energy Board Act, 1998, and in addition to a previous directive issued thereunder on August 10, 2006 by Order in Council No. 1537/2006, in respect of the Enbridge Undertakings and the Union Undertakings, I hereby direct the Ontario Energy Board to dispense,

- *under section 6.1 of the Enbridge Undertakings, with future compliance by Enbridge Gas Distribution Inc. with section 2.1 ("Restriction on Business Activities") of the Enbridge Undertakings, and*
- *under section 6.1 of the Union Undertakings, with compliance by Union Gas Limited with section 2.1 ("Restriction on Business Activities") of the Union Undertakings,*

in respect of the ownership and operation by Enbridge Gas Distribution, Inc. and Union Gas Limited, of:

- (a) renewable energy electricity generation facilities each of which does not exceed 10 megawatts or such other capacity as may be prescribed, from time to time, by regulation made under clause 71(3)(a) of the Ontario Energy Board Act, 1998 and which meet the criteria prescribed by such regulation;*
- (b) generation facilities that use technology that produces power and thermal energy from a single source which meet the criteria prescribed, from time to time, by regulation made under clause 71(3)(b) of the Ontario Energy Board Act, 1998;*
- (c) energy storage facilities which meet the criteria prescribed, from time to time, by regulation made under clause 71(3)(c) of the Ontario Energy Board Act, 1998; or*

(d) assets required in respect to the provision of services by Enbridge Gas Distribution Inc. and Union Gas Limited that would assist the Government of Ontario in achieving its goals in energy conservation and includes assets related to solar-thermal water and ground-source heat pumps;

(e) for greater certainty, the use of the word “facilities” in paragraphs (b) and (c) above shall be interpreted to include stationary fuel-cell facilities each of which does not exceed 10 Megawatts in capacity.

This directive is not in any way intended to direct the manner in which the Ontario Energy Board determines, under the Ontario Energy Board Act, 1998, rates for the sale, transmission, distribution and storage of natural gas by Enbridge Gas Distribution Inc. and Union Gas Limited.

3. Ownership Scenarios for Qualifying Facilities or Assets

This section provides an overview of two potential business scenarios for the ownership of qualifying facilities or assets.

The approach selected will determine the extent of regulatory oversight. These business scenarios are discussed in sections 3.1 and 3.2.

3.1. Qualifying Facilities or Assets Owned by an Affiliate

There are no legal or regulatory prohibitions imposed or enforced by the Board that preclude affiliates of natural gas utilities from owning and operating qualifying facilities or assets. However, if the affiliate intends to generate electricity for sale through the IESO-administered markets or directly to another person, the affiliate would require a licence from the Board pursuant to section 57 of the *OEB Act* unless exempt by regulation.

In addition, where a utility's affiliate owns and operates a qualifying facility or asset, the utility must comply with all applicable requirements of the Affiliate Relationships Code for Gas Utilities (“ARC”).

3.2. Qualifying Facilities or Assets Owned by Natural Gas Utility and Non Rate-Regulated

A natural gas utility may also choose to directly own and operate a qualifying facility or asset. Under this scenario, costs would not be recovered through rates and a regulatory return would not be earned on the investment. The investment

project or asset would be debt and/or equity financed. The utility may enter into a Feed-in Tariff contract with the Ontario Power Authority with respect to generation facilities. These contracts are long-term in nature and the contract prices vary depending on the type of generation technology and the capacity of the facility.

Like any other generator, a natural gas utility that chooses to generate electricity for sale through the IESO-administered markets or directly to another person is required to obtain a licence from the Board pursuant to section 57 of the *OEB Act* unless exempt by regulation.

4. Accounting Requirements

4.1. Qualifying Facilities or Assets Owned by a Natural Gas Utility's Affiliate

Under this ownership scenario, the utility will need only to review its policies, procedures and processes to ensure compliance with the ARC requirements. ARC requirements that the utility may need to consider include:

- A utility shall ensure accounting and financial separation from all affiliates and shall maintain separate financial records and books of accounts.
- Where a utility shares information services with an affiliate, all confidential information must be protected from access by the affiliate.
- A utility may provide loans, guarantee the indebtedness of, or invest in the securities of an affiliate, but shall not invest or provide guarantees or any other form of financial support if the amount of support or investment, on an aggregated basis over all transactions with all affiliates, would equal an amount greater than the specified percentage of the utility's total equity.

The allocation of costs consistent with applicable ARC requirements should be followed by the utility in developing its policies and procedures for allocating the cost of transactions, products or services between the utility and its affiliates.

To the extent possible, all direct and allocable costs between rate-regulated and non rate-regulated lines of business, services or products shall be traceable on the books of the regulated utility to the Uniform System of Accounts for Class "A" Gas Utilities ("Gas USOA"). Section 2.1.8 of the Natural Gas Reporting & Record Keeping Requirements (RRR) Rule for Gas Utilities ("RRR") contains the current reporting requirements for affiliate arrangements and transactions, and

section 2.2 of the RRR sets out certifications that must be provided annually in relation to ARC compliance. Furthermore, additional documentation shall be retained and made available to the Board upon request regarding transactions between the utility and its affiliates.

4.2. Qualifying Facilities or Assets Owned by Natural Gas Utility and Non Rate-Regulated

Although under this scenario utility activities pertaining to qualifying facilities or assets will not affect the setting of rates for the natural gas utility, the accounting treatment requires a segregation of these activities from the utility's rate-regulated activities. This segregation of information requires the use of specified accounts to record qualifying facility activities. A utility should follow these accounting procedures to ensure that information reported for rate setting purposes relates only to the utility's rate-regulated business and does not include the assets, liabilities, revenues and costs associated with its non rate-regulated activities. In this manner, the utility will continue to provide financial information on a "stand alone" rate-regulated basis in order to support the utility rate setting and other requirements of the Board.

Appendix B provides a methodology whereby a utility can allocate direct costs and a proportional share of indirect costs (such as payroll burden) to its non rate-regulated activities including its qualifying facility or asset business activities. Adhering to this methodology will ensure that utility ratepayers are not liable for non rate-regulated costs for which shareholders are responsible.

The utility should document and maintain records of its fully allocated costing methodology for qualifying facility or asset activities, including its application of this methodology to the accounts under the Gas USOA.

For accounting and reporting purposes, the utility would use the following asset, liability, shareholders' equity, revenue and expense accounts and sub-accounts to record transactions associated with non rate-regulated utility-owned qualifying facilities or assets.

- Account xxx, Non-Utility Plant in Service, Sub-account Qualifying Facility or Asset. Amounts recorded in this account shall include capital assets (property, plant and equipment) and intangible assets. These assets are not included in rate base and the associated amortization expenses are not included in the revenue requirement of the utility.

- Account xxx, Non-Utility Debt-Current, Sub-account Qualifying Facility Liabilities. Amounts recorded in this account shall include current liabilities associated with qualifying facilities or assets. These liabilities are not included in the utility rates.
- Account xxx, Non-Utility Debt-Non-Current, Sub-account Qualifying Facility Liabilities. Amounts recorded in this account shall include the liability portion not due within one year associated with qualifying facilities or assets. These liabilities are not included in the utility rates.
- Account xxx, Non-Utility Shareholders' Equity, Sub-account Qualifying Facilities. This sub-account shall include shares, paid-in capital, appropriated and unappropriated retained earnings, balance transferred from income and dividends associated with utility-owned qualifying facilities or assets. Sub-accounts may be used to distinguish the components of non rate-regulated shareholders' equity.
- Account 312, Non-Gas Operating Revenue, Sub-account Qualifying Facility Revenues. Amounts recorded in this account shall include revenues for qualifying facilities or assets from all sources, including Feed-in tariff contract revenues if applicable.
- Account 313, Non-Gas Operating Expense, Sub-account Qualifying Facility Expenses. Amounts recorded in this account shall include expenses associated with qualifying facilities or assets. Additional accounts shall be used under this sub-account to record the following categories of costs: (1) energy supply expenses (e.g. fuel), (2) operation, (3) maintenance (4) administration, (5) taxes and (6) amortization expenses.

A natural gas utility may use sub-accounts in addition to those specified in the above-noted accounts, as necessary to provide full details of the transactions related to utility-owned qualifying facility activities. Accounting information details should be maintained and made readily available to support Board review of these transactions.

These accounts are in effect for use to record transactions starting in 2010. The Board intends to include the above accounts in the Gas USOA as part of the updating of the Gas USOA related to the transition to International Financial Reporting System, and at that time will also assign numbers to those of the above accounts that currently have none. In addition, the Board intends to update the RRR section 2.1.7 USOA trial balance to include these accounts.

A natural gas utility is required to file annual audited financial statements under the RRR. The reporting requirements for financial statements in section 2.1.6 of the RRR specify the following:

...Where the financial statements of the corporate entity regulated by the Board contain material businesses not regulated by the Board, the utility shall disclose the information separately according to the segment disclosure provisions in the Canadian Institute of Chartered Accountants Handbook.

Where non rate-regulated activities are undertaken by the utility, the natural gas utility should ensure that any such activities that represent “material businesses” are reported as operating segments consistent with provisions of Section 1701, Segment Disclosures, of the Canadian Institute of Chartered Accountants Handbook in the utility’s audited financial statements. In addition, for rate setting purposes a utility will need to file financial information in rate applications that clearly delineates the utility’s rate-regulated activities from its non rate-regulated activities. The rate applications should provide a description of the procedures and processes that were used to segregate the accounting information.

Appendix A



Ontario
Executive Council
Conseil des ministres

Order in Council
Décret

On the recommendation of the undersigned, the Lieutenant Governor, by and with the advice and concurrence of the Executive Council, orders that:

Sur la recommandation du soussigné, le lieutenant-gouverneur, sur l'avis et avec le consentement du Conseil des ministres, décrète ce qui suit:

WHEREAS Enbridge Gas Distribution Inc. and related parties ("Enbridge") gave undertakings to the Lieutenant Governor in Council that were approved by Order in Council on December 9, 1998 and that took effect on March 31, 1999 ("the Enbridge Undertakings"), and Union Gas Limited and related parties ("Union") gave undertakings to the Lieutenant Governor in Council that were approved by Order in Council on December 9, 1998 and that took effect on March 31, 1999 ("the Union Undertakings");

AND WHEREAS the Minister of Energy and Infrastructure has the authority under section 27.1 of the *Ontario Energy Board Act, 1998* to issue directives, approved by the Lieutenant Governor in Council, that require the Ontario Energy Board to take steps specified in the directives to promote energy conservation, energy efficiency, load management and the use of cleaner energy sources including alternative and renewable energy sources;

AND WHEREAS The Government of Ontario has, with the passage of the *Green Energy and Green Economy Act, 2009*, embarked upon a historic series of initiatives related to promoting the use of renewable energy sources and enhancing conservation throughout Ontario;

AND WHEREAS certain amendments to the *Ontario Energy Board Act, 1998* provided for by the above-noted statute authorize electricity distribution companies to directly own and operate renewable energy electricity generation facilities with a capacity of ten (10) megawatts or less, facilities that generate heat and electricity from a single source, or facilities that store energy, subject to criteria to be prescribed by regulation;

AND WHEREAS it is desirable that both Enbridge and Union are accorded authority similar to those of electricity distributors to own and operate the kinds of generation and storage facilities referenced above, while clarifying that the latter two activities, namely the ownership and operation of facilities that generate heat and electricity from a single source, or facilities that store energy, are to be interpreted to include stationary fuel-cell facilities each of which does not exceed 10 Megawatts in capacity, as well as to allow Enbridge and Union the authority to own and operate assets required in respect of the provision of services by Enbridge and Union that would assist the Government of Ontario in achieving its goals in energy conservation including where such assets relate to solar-thermal water and ground-source heat pumps;

AND WHEREAS the Minister of Energy has previously issued a directive pursuant to section 27.1 in respect of the Enbridge Undertakings and the Union Undertakings, under Order-in-Council No. 1537/2006, dated August 10, 2006.

NOW THEREFORE the directive attached hereto is approved and is effective as of the date hereof.

Recommended: 
Minister of Energy
and Infrastructure

Concurred: 
Chair of Cabinet

Approved and Ordered: SEP 08 2009
Date


Lieutenant Governor

O.C. / Décret 1540 / 2009

MINISTER'S DIRECTIVE

Re: Gas Utility Undertakings Relating to the Ownership and Operation of Renewable Energy Electricity Generation Facilities, Facilities Which Generate Both Heat and Electricity From a Single Source and Energy Storage Facilities and the Ownership and Operation of Assets Required to Provide Conservation Services.

Enbridge Gas Distribution Inc. and related parties gave undertakings to the Lieutenant Governor in Council that were approved by Order in Council on December 9, 1998 and that took effect on March 31, 1999 ("the Enbridge Undertakings"); and Union Gas Limited and related parties gave undertakings to the Lieutenant Governor in Council that were approved by Order in Council on December 9, 1998 and that took effect on March 31, 1999 ("the Union Undertakings").

The Government of Ontario has, with the passage of the *Green Energy and Green Economy Act, 2009*, embarked upon a historic series of initiatives related to promoting the use of renewable energy sources and enhancing conservation throughout Ontario.

One of those initiatives is to allow electric distribution companies to directly own and operate renewable energy electricity generation facilities of a capacity of not more than 10 megawatts or such other capacity as is prescribed by regulation, facilities which generate both heat and electricity from a single source and facilities for the storage of energy, subject to such further criteria as may be prescribed by regulation.

The Government also wants to encourage initiatives that will reduce the use of natural gas and electricity.

Pursuant to section 27.1 of the *Ontario Energy Board Act, 1998*, and in addition to a previous directive issued thereunder on August 10, 2006 by Order in Council No. 1537/2006, in respect of the Enbridge Undertakings and the Union Undertakings, I hereby direct the Ontario Energy Board to dispense,

- under section 6.1 of the Enbridge Undertakings, with future compliance by Enbridge Gas Distribution Inc. with section 2.1 ("Restriction on Business Activities") of the Enbridge Undertakings, and
- under section 6.1 of the Union Undertakings, with future compliance by Union Gas Limited with section 2.1 ("Restriction on Business Activities") of the Union Undertakings,

in respect of the ownership and operation by Enbridge Gas Distribution, Inc. and Union Gas Limited, of:

- (a) renewable energy electricity generation facilities each of which does not exceed 10 megawatts or such other capacity as may be prescribed, from time to time, by

regulation made under clause 71(3)(a) of the *Ontario Energy Board Act, 1998* and which meet the criteria prescribed by such regulation;

- (b) generation facilities that use technology that produces power and thermal energy from a single source which meet the criteria prescribed, from time to time, by regulation made under clause 71(3)(b) of the *Ontario Energy Board Act, 1998*;
- (c) energy storage facilities which meet the criteria prescribed, from time to time, by regulation made under clause 71(3)(c) of the *Ontario Energy Board Act, 1998*; or
- (d) assets required in respect of the provision of services by Enbridge Gas Distribution Inc. and Union Gas Limited that would assist the Government of Ontario in achieving its goals in energy conservation and includes assets related to solar-thermal water and ground-source heat pumps;
- (e) for greater certainty, the use of the word "facilities" in paragraphs (b) and (c) above shall be interpreted to include stationary fuel-cell facilities each of which does not exceed 10 Megawatts in capacity.

This directive is not in any way intended to direct the manner in which the Ontario Energy Board determines, under the *Ontario Energy Board Act, 1998*, rates for the sale, transmission, distribution and storage of natural gas by Enbridge Gas Distribution Inc. and Union Gas Limited.



George Smitherman
Deputy Premier, Minister of Energy and Infrastructure

Appendix B

Fully Allocated Costing Methodology for Non Rate-Regulated Activities

1. DEFINITIONS

In this Appendix:

"Allocable Costs" means indirect costs (i.e., costs that would be incurred regardless of whether or not the Non Rate-Regulated Activities were undertaken);

"Cost Driver" means a measure used to allocate, to a Non Rate-Regulated Activity, the costs of any functions performed within the utility to undertake that Non Rate-Regulated Activity;

"Fully Allocated Costs" means the sum of Marginal Costs and Allocable Costs;

"Marginal Costs" means direct costs (i.e., costs that would be eliminated or reduced if the Non Rate-Regulated Activities were no longer undertaken); and

"Non Rate-Regulated Activities" means activities that are carried out by a utility but not rate-regulated by the Board.

2. COST ALLOCATION PROCESS

2.1 Marginal Costs can be directly assigned to the Non Rate-Regulated Activity. Allocable Costs must be allocated, using a Cost Driver, to determine the proportional share of the Allocable Costs attributable to the Non Rate-Regulated Activities.

2.2 In order to determine the costs associated with the Non Rate-Regulated Activities, utilities shall use an activity analysis to assess the nature and extent of the functions being performed throughout the utility to undertake the Non Rate-Regulated Activities. The analysis must include the identification of all activities performed within the utility regardless of whether or not these activities directly or indirectly support the Non Rate-Regulated Activities.

2.3 The activity analysis referred to in section 2.2 must include the following Marginal Costs and Allocable Costs, where applicable:

- (a) all salaries and labour costs including benefits;
- (b) contractor expenses;
- (c) billing and collection;
- (d) customer care, marketing and advertising;
- (e) administration and general expenses;
- (f) IT costs;
- (g) office equipment; and
- (h) any other cost that the utility can show is relevant and necessary for the program analysis.

2.4 A utility must determine an appropriate Cost Driver for each Allocable Cost. Cost Drivers must be:

- (a) representative of how costs are being incurred;
- (b) implemented in a cost effective manner; and
- (c) verifiable and justifiable.

The types of Cost Drivers that utilities may use are included below in sections 2.5 to 2.7.

2.5 Utilities may use headcount as a Cost Driver for the allocation of salaries, other labour related costs, administration and general expenses, and IT costs. This Cost Driver is based on the number of full-time equivalents needed to support the Non Rate-Regulated Activities. Utilities shall calculate full time equivalents in accordance with the following examples:

- (a) if six employees each devoted 25% of their time to the Non Rate-Regulated Activity, the full-time equivalent for those employees would be 1.5; and
- (b) if six part-time employees each devoted 25% of their time to the Non Rate-Regulated Activities, the part-time positions would first need to be translated into a full-time position (i.e., if an employee works 3 days per week, the full-time position would be 0.6) and then apply the percentage (i.e., $6 \times 0.6 = 3.6$ and 25% of $3.6 = 0.9$) so the full-time equivalent would be 0.9.

2.6 Utilities may use time as a Cost Driver for the allocation of executive and administrative functions, legal services, and financial analysis because these functions are typically project specific. Utilities shall calculate the percentage of time to be allocated to the Non Rate-Regulated Activities by using the base hours per employee. A utility shall calculate an employee's base hours by determining the hours that the employee can be considered

to be available for work for the period being measured. Utilities shall calculate the percentage of time in accordance with the following example:

- (a) if an employee's base hours are 40 hours per week and the employee actually worked 40 hours that week, which included four hours of his/her time spent on a Non Rate-Regulated Activities, the percentage of time allocation would be 10 percent; and
- (a) If an employee's base hours are 40 hours per week and the employee actually worked 60 hours that week, which included four hours of his/her time spent on a Non Rate-Regulated Activities, the percentage of time allocation would still be 10 percent.

- 2.7 Utilities may use the frequency of an activity as a Cost Driver for the allocation of call centre costs and accounts payable processing because these activities can be repetitive in nature and consistent over time in terms of the level of effort required to provide the service. Call centre costs shall be allocated based on number of calls received in relation to the Non Rate-Regulated Activities and accounts payable processing costs shall be allocated based on the number of invoices processed for Non Rate-Regulated Activities.