

Chapter 3

Section 3.07

Ontario Energy Board— Natural Gas Regulation

Background

The Ontario Energy Board (Board) was established in 1960 as a quasi-judicial administrative tribunal, charged with regulating the province's natural gas sector in the public interest. Over time the Board's authority expanded to also include oversight of the electricity sector. The Board operates under the authority of the *Ontario Energy Board Act, 1998*, and is responsible to ensure that natural gas market participants comply with the *Energy Consumer Protection Act, 2010* (specifically those selling to low-volume users, i.e., users who annually use less than 50,000 m³ of gas). The *Municipal Franchises Act* sets out the requirements for the allocation of municipal service territories to the regulated utilities.

The *Ontario Energy Board Act* sets out specific board objectives for natural gas services and systems, including:

- to facilitate competition in the sale of gas to users;
- to protect the interests of consumers with respect to prices and the reliability and quality of gas services;
- to facilitate rational expansion of transmission and distribution systems, and development and safe operation of gas storage; and

- to promote energy conservation and energy efficiency.

The Board's key functions in achieving these objectives cover:

- setting prices for natural gas, its delivery and storage;
- licensing of gas marketers and oversight of natural gas market participants, including both gas utilities and gas marketers, for compliance with applicable legislative and policy requirements; and
- reviewing and setting codes, rules and guidelines.

In Ontario, residential consumers have the option of purchasing their natural gas from either a gas utility or one of 12 gas marketers actively selling natural gas. There are three utilities that own the pipes and equipment that deliver the natural gas to a home or business, plus two municipal utilities that also distribute natural gas. Each utility serves different territories across the province. With the granting of a Certificate of Public Convenience and Necessity, the Board gives a particular utility an exclusive right to supply gas and to expand gas service within a municipality. This utility must then enter into a Municipal Franchise Agreement with the municipality to service its consumers and maintain its infrastructure within the municipality.

The Board regulates the rates that the three utilities charge their consumers, but not those that the gas marketers charge. The gas marketers operate as brokers, locating natural gas on the market to sell competitively. When consumers purchase gas from marketers, they enter into fixed-term contracts for periods of one to five years. If consumers do not enter into contracts with gas marketers, they get their gas supply from a utility, which is the default supplier.

For the year ended March 31, 2014, there were 3.5 million natural gas customers in Ontario. Of these, 3 million purchased their gas from one of the three utilities; this number included about 14,000 high-volume consumers as well as the majority of low-volume consumers who annually consume 50,000 m³ or less of gas. Two of these utilities supplied more than 99% of the total natural gas consumption in Ontario. In addition, about 404,000 low-volume consumers collectively purchased gas from the 12 gas marketers actively selling gas.

The Board conducts its regulatory oversight function through a quasi-judicial process that allows for public participation. Panels of board members hold both oral and written regulatory proceedings, which must comply with established laws and board rules. Panel decisions must uphold the broad public interest, which includes the protection of consumers, the financial integrity of the utilities and other legislative goals such as safe operation of storage and energy conservation.

There are many parties to a regulatory proceeding: the applicant; the board panel as the decision-makers; board staff to support the panel or to act with delegated decision-making authority; and intervenors. The intervenors are individuals or groups who represent residential, institutional, commercial and large industrial consumers of energy, as well as environmental and policy advocacy groups. They include the Vulnerable Energy Consumers Coalition, the School Energy Coalition, the Consumers Council of Canada, the Industrial Gas Users Association and many others. Intervenors actively participate in applications,

policy consultations and other proceedings before the Board, supporting the Board in its regulatory proceedings by submitting arguments or written questions, or by cross-examining witnesses.

The Board uses a three-stage process in regulating natural gas rates. One stage requires utilities to submit a cost of service application approximately every five years, which establishes the base rates to charge consumers. The utilities provide information on the estimated demand as well as estimated capital and operating costs to serve the forecast demand; the rates they can charge include a Board-approved return on their capital investments. A second stage reviews and adjusts the gas rates annually between cost of service reviews, typically using a formula that considers inflation adjusted by the utilities' productivity figures. A third stage adjusts gas rates four times a year through a quarterly rate adjustment mechanism to smooth out fluctuations in billing rates and reflect current market prices for natural gas, as well as, for example, changes in the transportation rates and changes in inventory valuations.

At the conclusion of its review processes the Board issues its decision through an Order. For the fiscal year ending March 31, 2014, the Board issued 53 decisions arising from oral and written hearings for natural gas, of which 13 decisions related to utilities' rates and the remainder related to facilities and licensing.

As of March 2014, the Board had nine members—six part-time and three full-time, appointed by the Lieutenant Governor in Council. The Board's daily operations are carried out by a staff of about 160. (See **Appendix** for the Board's organizational chart.) All regulatory costs, including intervenor costs, are recovered from the regulated and licensed entities. Board costs in the 2013/14 fiscal year to regulate the gas sector were \$5.9 million of the \$33.2 million total board operating costs. Gas utilities contributed \$5 million, and gas marketers contributed \$900,000. The 2011/12 fiscal year was the first year in which the gas marketers were required to cover a portion of the Board's costs.

Audit Objectives and Scope

The objective of our audit was to assess whether the Ontario Energy Board had effective systems and processes to protect the interests of natural gas consumers and ensure that the natural gas sector provides energy to consumers at a reasonable cost.

Our audit focused on areas that directly impact the consumer in terms of rates charged, oversight and monitoring of the compliance of utilities and gas marketers to legislative and Board requirements, and the quality of services provided to consumers by gas utilities and gas marketers.

In conducting our audit, we reviewed relevant legislation as well as administrative policies and procedures, and we interviewed staff at the Board, the Ministry of Energy, and the Ministry of Natural Resources and Forestry. Our audit focused on the Board's review of the two largest gas utilities, which supplied over 99% of the natural gas consumed in Ontario. To gain an overall understanding of and perspective on the natural gas sector, we spoke with the regulated gas utilities, and a number of gas marketers and intervenors. We also contacted and conducted research into the operations of similar regulatory agencies in other Canadian and foreign jurisdictions. In addition, we engaged the services of an independent consultant with expertise in the regulation of the natural gas sector to assist us on an advisory basis.

Prior to the commencement of the audit, we developed audit criteria. These audit criteria were reviewed and agreed to by the Board's senior management.

We conducted our fieldwork from late November 2013 through to the end of April 2014.

Summary

The Ontario Energy Board has adequate systems and processes in place to protect the interests of natural gas consumers and ensure that the natural gas sector provides energy at a reasonable cost. However, more can be done to demonstrate board effectiveness. We noted that board staff need to more fully assess the different approaches used by the utilities in recovering their costs, which affect the rates they are able to charge their customers. The Board also needs to more fully verify the accuracy and validity of the information provided by the utilities when they apply to the Board for rate changes.

Some of our key observations are as follows:

- More thorough review of utilities' documents and processes that affect consumer rates needed:** Gas utilities are not allowed to charge consumers more than the purchase cost of gas. However, board staff seldom obtained source documents to verify the information the utilities provided in rate change applications. Board staff did not conduct sufficient reviews of the critical gas cost adjustment accounts, processes for gas purchases and transportation contracts. These costs are passed through to consumers and significantly impact consumer rates. The Board has the right to request information supporting the prudence of the utilities' gas purchases, and if it examined and compared this information between utilities, it might be able to help identify best practices for the utilities to follow. We noted that over the last 10 years only one audit of gas cost adjustment accounts and accounting processes was done, in 2011, and on only one utility. Board staff had not conducted a similar review for the other two regulated utilities since 2000. The 2011 audit identified concerns such as the utility not documenting justification for purchasing gas

from suppliers who offered prices that were higher than the lowest bid prices, not having a clear policy for when competitive purchasing was required, and not complying with the commitment it made to the Board in 2000 to update documentation of its gas cost system procedures (updating was subsequently completed by December 2011).

The two utilities that supply over 99% of the gas consumed in Ontario have affiliated companies that also provide gas in other jurisdictions. Without sufficiently examining actual purchase records of these two utilities, the Board might not have taken sufficient care to protect Ontario consumers from the possibility of inappropriate charges (for example, misallocated costs relating to other provinces) being passed through to them.

- **Inadequate evaluation of recovery methods' impact on consumer gas rates:** The gas utilities apply different approaches to recover their Board-approved revenue requirement. However, board staff have not assessed the impact that these differences have on consumers. Utilities recover their approved service costs and rate of return on capital through fixed monthly charges and usage-based charges to customers. Board staff indicated that as long as the approved total costs are collected, it is up to the utilities to propose how much to recover through each charge. A utility's decision to give more weight to fixed rather than usage-based charges, however, could disadvantage consumers who do not have high gas usage, as they pay more for each unit of gas when more of the cost recovery is taken on fixed charges than on usage.
- **Insufficient consumer information on gas marketers' rates:** Complaints against gas marketers decreased by 81% from 2009 to 2013. (Unlike utilities, marketers charge unregulated consumer rates.) However, we noted that contract cancellation and renewal issues were still frequent consumer complaints, as consumers

often discovered that they could pay lower prices with other gas providers. Providing consumers with rate information from the various gas providers would enable consumers to make more informed decisions before entering into a contract.

- **Few utility performance measures:** The Board had some customer-based performance measures in place to assess the natural gas utilities' performance, but would benefit from applying additional performance measures, such as measures relating to operational effectiveness, financial performance and public policy responsiveness.
- **Lack of reviews of board effectiveness:** The *Ontario Energy Board Act, 1998* enables the Minister of Energy to require a report be prepared every five years on the Board's effectiveness in meeting its many mandated objectives such as facilitating competition in the sale of gas and encouraging energy conservation and energy efficiency. No ministry reviews of the Board's effectiveness have been done since the *Ontario Energy Board Act 1998* came into effect.

OVERALL BOARD RESPONSE

The Board welcomes the conclusion of the Auditor General that the Board has adequate systems and processes in place to protect the interests of natural gas consumers and ensure that the natural gas sector provides energy at a reasonable cost. The Board is committed to assessing and improving its own performance and effectiveness and, in that regard, welcomes the recommendations of the Auditor General. As set forth in further detail below, the Board accepts all the recommendations.

Detailed Audit Observations

Regulating Gas Utilities

The Ontario Energy Board (Board) has developed adequate systems and processes to protect the interests of natural gas consumers and ensure that natural gas is provided to consumers at a reasonable cost. The processes that the Board has in place for setting and adjusting rates have kept consumer costs in line with market prices for the gas. Overall, Ontario consumers pay less for natural gas than those in all but one province and parts of two others. However, we are concerned that board staff have made insufficient efforts to analyze and assess the different approaches used by the utilities in assigning their rates. Board staff have also made insufficient efforts to verify the accuracy and validity of the information that utilities submit in their rate increase applications to support the Board in its decision-making.

The Board's regulatory functions are especially important in the current situation in which the two largest utilities in Ontario supply over 99% of the gas consumed in the province.

The Consumer's Monthly Gas Bill

Consumers in Ontario can get a glimpse at the complex pricing mechanism for their natural gas purchases by looking at their monthly gas bill. The customer gas bill includes monthly fixed charges and usage-based charges. The usage-based charges for a typical residential customer are as follows:

- **Gas supply charge**—a forecast of market prices for the next 12 months. Added to this charge are gas supply-related costs such as compressor fuel costs, system gas fees, working cash requirements and customer bad debt, all of which are approved by the Board. These gas supply-related costs vary by utility, but represented up to 4% of the costs in the April 2014 quarterly rate adjustment mechanism for the two large utilities.

- **Delivery cost**—which has three components:
 - Transportation charge—the cost of transporting gas to Ontario from western Canada and the United States. Transportation rates are determined by the National Energy Board in Canada and U.S. regulatory authorities in the United States, and are charged to customers.
 - Distribution charge—the cost of delivering natural gas in the utility's territory to the customer's home. This charge also includes all operating and maintenance costs and a rate of return.
 - Storage charge—the cost to the utility of storing its natural gas.
- **Cost adjustment charge**—which tracks the difference between the actual and forecast price of gas and the resulting impact on other charges, such as gas inventory in storage, costs of balancing gas supply to meet demand, and transportation costs.

Figure 1 shows the above components in a model of the monthly bills sent out by the two large utilities on April 1, 2014, to customers with an average monthly gas consumption of 255 m³. Utility A serves a small number of compact and relatively

Figure 1: The Consumer's Monthly Gas Bill, April 1, 2014¹ (Usage 255 m³)²

Source of data: OEB

| | Adjusted Quarterly Rate (\$) | | |
|-------------------|------------------------------|-------------------------|--------------|
| | Utility A | Utility B (Southern) | Difference |
| Customer charge | 20.00 | 21.00 | (1.00) |
| Gas supply charge | 44.89 | 45.70 | (0.81) |
| Delivery charge | | | |
| Distribution | 29.72 | 9.41 | 20.31 |
| Transportation | 12.13 | 8.80 | 3.33 |
| Storage | — | 1.88 | (1.88) |
| Cost adjustment | 8.40 | 11.40 | (3.00) |
| Total | 115.14 | 98.19 | 16.95 |

1. Model monthly natural gas bill for April 1, 2014, based on the bills sent out by Ontario's two largest gas utilities.
2. For purposes of comparison, gas usage of 255 m³ is taken here as average monthly usage for a consumer household.

densely populated territories located mostly in southern and eastern Ontario. Some of the territories served by Utility B are comparable to those of Utility A, but Utility B also serves a number of widespread and relatively lightly populated territories across the south and the north of the province and divides its territories into five zones in which consumers may pay five different rates due to different costs of transportation, distribution and storage (see **Figure 2**). (For more details, see the section “Differing Regional Rates Paid in Ontario.”)

Natural Gas Prices Appear Reasonable Overall

To determine if Ontario’s residential customers are being charged reasonable natural gas prices, we (1) reviewed the prices paid by residential

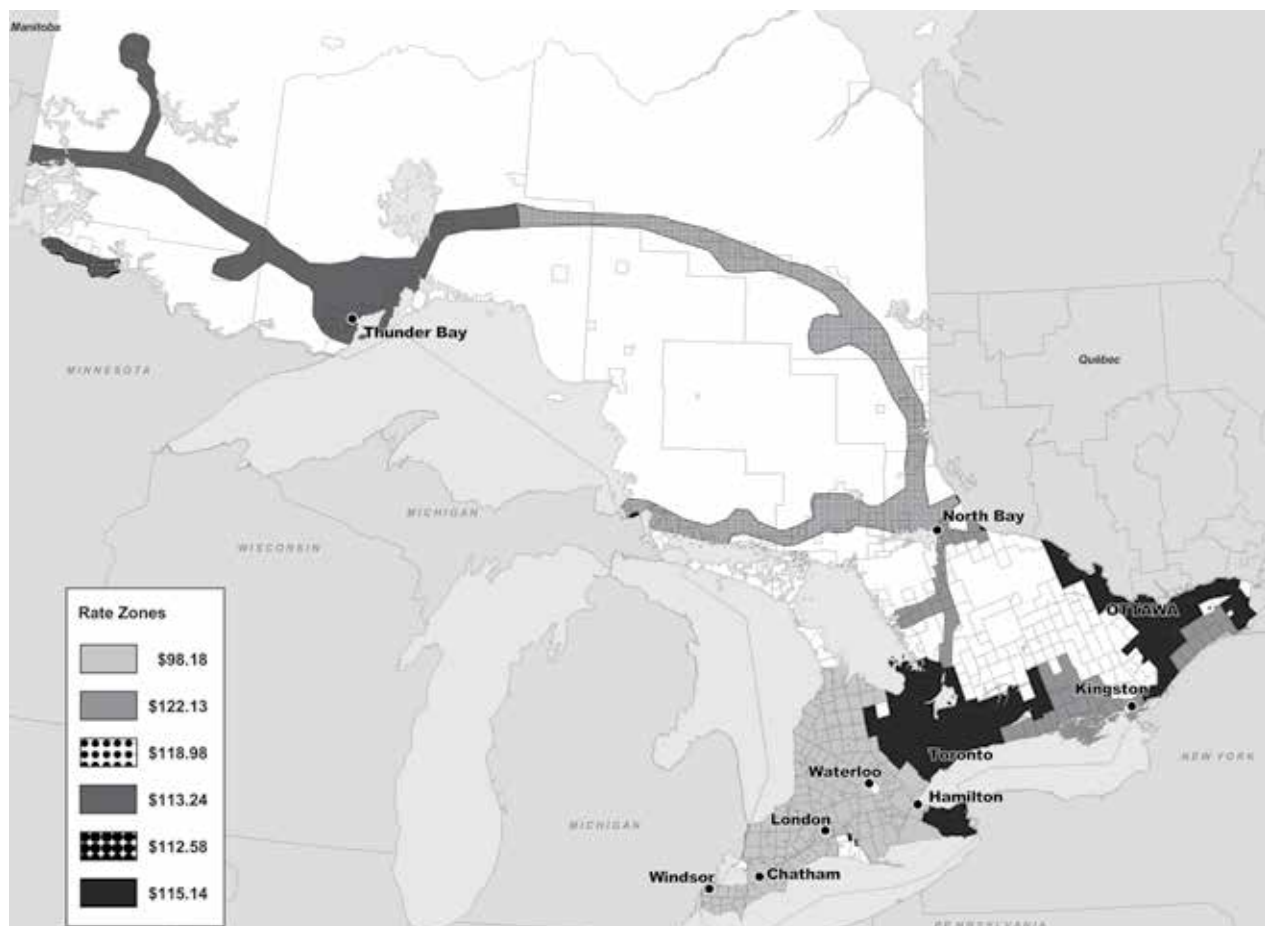
customers in other Canadian jurisdictions; (2) compared consumer gas supply prices to a standard based on the price charged on the commodity exchange for gas over time; and (3) looked at the quarterly rate adjustment process that allowed Utility A an interim price increase of 40% following the unusually cold winter of 2013/14.

Only One Province and Parts of Two Others Price Natural Gas Lower Than Ontario

Ontario’s gas prices are at the low end of the range of prices available across Canada. Assuming an average monthly household gas consumption of 255 m³, in April and May 2014 only Saskatchewan (which operates its utility as a Crown corporation) and parts of Alberta and British Columbia had

Figure 2: Utility Gas Distribution Areas and Gas Rates for a Residential Customer with a Monthly Consumption of 255m³ of Gas, April 2014

Source of data: OEB



prices that were lower than the prices charged to 99% of Ontario's gas consumers by Ontario's two largest utilities.

Ontario Consumer Gas Prices Are in Line with the Commodity Exchange Price

In Ontario, regulated utilities are not allowed to make a profit on the transportation of natural gas and its sale as a commodity to consumers. The gas utilities are to charge customers their actual purchase cost of gas and their actual cost of transporting it to Ontario. To verify that the cost consumers pay for the gas itself (known as the gas commodity rate) fairly reflects the cost the utilities paid in purchasing the gas, we compared the gas rates of the two largest utilities, which supplied over 99% of Ontario's natural gas consumption, to the average price of the gas available to the utilities for purchase in Alberta. The Alberta price (known as the Empress price) is the basis for establishing the cost of gas to the utilities that the Board approves as the reference price.

For the utilities' purchase prices we used the calculated 21-day average of the forecast of the upcoming 12 months' prices to arrive at the Board-approved reference prices for the years from January 2007 to April 2014. We noted that the rates the utilities charged consumers for the gas were closely aligned to the Empress prices over this time period. Based on this review, we are satisfied overall that, for the gas they supplied, the two large utilities charged consumers prices that reflected natural gas market prices.

Assessment Process Followed Properly in April 2014 Quarterly Gas Rate Adjustment

The rates that the utilities may charge their customers for the gas supply itself are adjusted each quarter and come into effect on January 1, April 1, July 1 and October 1 of each year. The underlying principles of these adjustments are to more accurately reflect market prices on an ongoing basis; provide enhanced price transparency; smooth out

large adjustments on customers' bills; and provide fairness and equity among customer groups, such as residential, small commercial and high-usage customers. The quarterly rate adjustment review and approval process is expected to take approximately two weeks. Board staff are delegated the authority to assess and approve the utilities' quarterly rate adjustment applications. In complex cases, such as those involving policy or unusually high adjustments, the applications are adjudicated before the board panel.

Record cold temperatures in the winter of 2013/14 led to Ontario's two largest utilities requesting exceptionally high rate increases in the April 2014 quarterly rate adjustment. Following the decision of a board adjudication panel, the Board granted Utility A an interim 40% increase and Utility B a 28% increase. These price increases provoked a strong reaction from consumers and the media. Our audit looked at how the Board reached its decisions, with a focus on the question of whether the two rate increases were supported by the information the Board was given.

Based on our review, one of the main reasons that Utility A's April prices increased more than Utility B's was that its gas plan was very different from Utility B's gas plan. Both plans were approved by the Board.

Gas plans define the gas supply requirements and transportation capacity needed to deliver natural gas to Ontario users, and list the assets available to meet customers' demand for annual and seasonal gas delivery. The plans also make provision for gas delivery on extreme low-temperature days (peak demand days). Information necessary to estimate the demand includes data on weather, firm customer demand and forecast demand growth.

We reviewed the April 2014 quarterly rate adjustment applications for the two largest utilities, which were adjudicated by the board panel and reviewed by board staff. We also reviewed queries by board staff and intervenors, and the utilities' responses to those queries.

Our review of the applications noted that the utilities' requests for rate increases were due to significantly higher demand arising from the most recent winter's long period of severely cold temperatures, which significantly increased the gas supply costs. One utility pointed out that this was a one-in-35-year occurrence.

Documents furnished to the Board provided reasons for the rate increase requests. Utility A, the utility with the higher quarterly rate increase, attributed the increase to a number of supply, delivery and cost-adjustment factors. Its gas supply plan maintains maximum storage capacity for gas delivery to January 31, while Utility B, the utility with more storage, maintains maximum capacity for delivery until March 1 each year. Therefore, Utility A could not store the same quantity of gas as Utility B. Its declining stores of gas ready to deliver in February forced it to make more short-term gas purchases in the daily market when demand was higher and where prices are higher.

Based on the normal quarterly rate adjustment process, the utility filed an application seeking a rate adjustment to pass through to customers the actual higher gas costs incurred due to these exceptional weather conditions. Utility A indicated in its responses to board staff and intervenors that if its gas supply plan had been the same as Utility B's plan, it could have saved about \$150 million in lower gas prices it would have paid by making its additional purchases on a more advantageous schedule.

In addition, if Utility A could have maintained its stores of gas ready to deliver until the end of February and eliminated peak-demand services, it could potentially have saved an additional \$71 million on top of the \$150 million cost of the gas itself.

We concluded that the Board's processes were followed properly and resulted in decisions that can be supported. We also noted that the Board issued a Decision and Order on May 22, 2014, to mitigate the significant impact of the rate increase on consumers by approving a 27-month rate smoothing period rather than the normal 12-month period.

This extended period lessened the impact of the price increase on the utility's customers.

Although the April 2014 rate increase approved for Utility A was higher than the one approved for Utility B, our review of the quarterly effective prices for the two large utilities from 2006 to 2014 showed that no one utility had prices that were consistently lower or higher than the other utility's prices over this time period.

Following our audit fieldwork, in June 2014 the Board began a two-phase review of the quarterly rate adjustment mechanism for natural gas distributors to address any similar situations that could arise in future. The first phase will include a review of the process, including the filing of the application and supporting evidence, triggers for a substantive review, and timelines for review and comments. It will also include a review of the Board's policy on smoothing rate increases on the customer's bill and a review of its protocols for communicating with consumers.

Evaluation of Differences in Consumer Gas Rates

Differing Regional Rates Paid in Ontario

Natural gas rates charged to residential customers by the two large utilities differ across the province. Utility A, serving a smaller number of more densely populated residential regions, charges all of its residential customers a single provincial rate. In contrast, Utility B, which serves several widespread and lightly populated territories in addition to some densely populated residential regions, charges five different gas rates depending on the location of the customer. This results in a situation where one consumer located in close proximity to another could pay substantially more, as illustrated in **Figure 2**. For instance, in southern Ontario, in April 2014 a residential consumer with Utility A paid \$115.14 for 255 m³ of natural gas, while a residential consumer living nearby in Utility B's southern zone and using the same amount of gas paid only \$98.19.

A simple average of the monthly bills of all residential customers of both Utility A and Utility B with gas consumption of 255 m³ per month would give their customers a single province-wide monthly bill of \$113.38. This would benefit customers in the two zones of Utility B that pay higher rates, and all customers of Utility A, with increased payments for customers in two other zones of Utility B. (There would be almost no change to customers in one other zone.) Calculating a provincial average for the Board to enforce would have customers in some areas of the province subsidizing the higher costs that customers in other areas currently pay for their service. The utilities' costs of supplying natural gas currently differ across the province due to different costs of transportation, distribution (building infrastructure to deliver gas to customers) and storage. These costs are affected by many factors, such as large geographical distances over which the utilities transport gas, population densities of the different areas they serve, the utilities' storage capacities, the kinds of assets they use (cast iron versus steel or plastic mains) and other factors.

Cost of Service Reviews Do Not Take into Account All Information and Practices That Could Affect Consumer Rates

As noted earlier, we found that the April 2014 quarterly gas supply rate adjustments applied to the consumer bill were reasonable. The other components of the consumer gas bill include fixed monthly charges, transportation, delivery and storage charges. These components are determined and adjusted through the cost of service application process review, and usually adjusted in incentive regulation or quarterly rate adjustment applications. Approximately every five years, in accordance with the Board's 2005 Minimum Filing Requirements, regulated utilities submit to the Board a full cost of service application that includes details of their operating revenues for the future year, current year and previous year; estimated demand for their

gas; estimated capital costs and operating costs to serve the forecast demand; and estimated rate of return that they request the Board to approve on their capital investments. The Board uses this information to determine the amount of money each utility is permitted to earn (known as its revenue requirement), which the utilities use to set their fixed monthly charges and usage-based charges.

Board staff rely on policy and previous adjudication decisions and board procedural manuals in their review of these cost of service applications. We reviewed the most recent cost of service applications effective for the 2013 rates for the two largest utilities. Board staff and intervenors requested many additional supporting schedules or clarifications of information provided in the applications to aid in their review, although board staff did not regularly evaluate and compare differences between the two utilities in information and practices that could have an impact on the consumer gas bill. These include the different cost structures used by the two utilities, their different rate designs (the weighting of fixed versus usage charges) and the different costs each utility pays for its gas supply.

Rate designs could disadvantage some customers

In reviewing cost of service applications, board staff have not compared the information submitted by the two utilities to assess the differences and the potential impact on consumer rates, or to help identify best practices. In particular:

- **Differences in delivery charges:** As noted in **Figure 1**, the greatest variation between the total monthly charge to residential customers of Utility A and those of Utility B (zone 1) was in the delivery charge, a \$20.31 (216%) difference. We noted that this difference includes a gas cost adjustment of \$10.23 for Utility A from a prior period. Nevertheless, board staff did not conduct or request a comparison of the differences in the two utilities' delivery capabilities and the cost impact on customers.

According to board staff, delivery-related charges differ due to the underlying different

distribution-related costs to serve customers of Utility A and Utility B, including factors such as age and composition of assets, population density in customer-service areas, and company operating costs. However, board staff were unable to provide a breakdown of these differences.

- **Lack of clarity in rate designs:** The delivery charge is also affected by the utility's rate design. The rate design determines the proportion of the utility bill recovered through fixed monthly charges and the proportion recovered through usage-based charges. Utilities recover their fixed costs through fixed charges and the remainder of their permitted earnings through usage-based charges. To be able to determine the reasonableness of the amounts recovered by utilities from fixed charges, there needs to be a clear breakdown of costs and charges that links the fixed costs to the charges. We found that there was no clear linkage of the utilities' fixed costs to support the amounts collected through fixed charges.
- **Different weighting of fixed and usage-based charges:** The two utilities' cost recovery practices showed significant differences in the percentages they took in fixed charges and in usage-based charges billed to residential consumers. In the most recent (2013) cost of service application, for its residential consumer billing, Utility B forecast recovery of \$266.8 million of \$282.1 million, or 95%, in fixed consumer-related costs such as meter reading, administration of accounts and infrastructure (77% recovered in its 2007 cost of service application); Utility A forecast recovery of \$447.97 million of \$363.13 million, or 123%, of such costs (71% recovered in 2007).

Such differences in the weighting of cost recovery between fixed and usage-based charges could present inequities that disadvantage consumers who do not have high usage of gas, as they pay more for each unit of gas when

more of the cost recovery is taken on fixed charges than on usage charges.

Settlement proposals are not reviewed from a public interest perspective

According to board staff, in their respective 2008 rate applications, the percentages of the utilities' costs that the utilities are permitted to recover through customer billing were determined in a settlement process involving the utilities and the intervenors. In a rate application, the Board normally requests the participating parties to reach agreement through the settlement process, if possible. This avoids a full-scale hearing before the Board; only those issues on which agreement has not been reached are heard through board proceedings. The goal of this less formal settlement process is to achieve regulatory efficiency. At the end of the process, the intervenors and the utility file with the Board a proposal describing their agreement to the issues.

Board staff indicated that they had not evaluated the different costing methodologies used in the settlements, as their role in the settlement process is limited to ensuring compliance with board requirements. Thus, board staff did not participate in assessing the appropriateness of the settled recovery percentages referred to earlier. However, during the settlement conference, board staff are required to present options for the consideration of the parties and to offer advice on the strengths and weaknesses of the parties' proposals. Our review showed there was no board staff submission commenting on whether the settlement proposal represents an acceptable outcome from a public interest perspective, and whether the accompanying explanation and rationale are adequate to support the settlement proposal.

RECOMMENDATION 1

To ensure that its regulatory decisions protect the interests of natural gas consumers and the public interest, and that the natural gas sector

provides gas to consumers at a reasonable cost, the Ontario Energy Board should:

- compare the different cost recovery approaches applied by the regulated utilities;
- compare information submitted by the utilities and identify best practices in purchase, transport and storage of gas that could have an impact on consumer rates;
- implement any needed changes arising from its review of the quarterly gas rate adjustment process that it began in June 2014; and
- assess whether the settlement proposal represents an acceptable outcome from a public-interest perspective, and whether the accompanying explanation and rationale are adequate to support the settlement proposal.

BOARD RESPONSE

The Board accepts this recommendation.

The Board notes that the first phase of the review of the quarterly rate adjustment mechanism (QRAM) was completed in August 2014. Going forward, the Board will require each gas distributor to use best efforts to ensure that customers are made aware in a timely manner if the anticipated increase in the gas supply component of bills for residential customers exceeds 25%.

The second phase of the Board's review of QRAM will follow the Natural Gas Market Review forum scheduled for December 2014. That second phase will examine the gas supply plans used by the gas distributors, including the different ways in which commodity price and risk are addressed in those plans.

The Board also notes it amended its Practice Direction on Settlement Conferences regarding the role of board staff in respect of settlement proposals in April 2014. In accordance with these amendments, board staff now make submissions to the presiding board panels on settlement proposals addressing the very factors identified by the OAGO. The Board acknowledges that these guidelines were not in place at the time of the 2013 proceedings noted by the OAGO.

Additional Review Needed for Accuracy and Validity of Information Submitted to the Board

Our review of the quarterly gas rate adjustment application process noted that utilities provided different levels of support for their pricing requests and applied different approaches in arriving at information required to be submitted. Board staff do not compare the approaches used by the utilities. We found as well that board staff seldom obtained source documents to assess the information provided in the various applications for accuracy and validity.

For example, when determining their gas supply rates for the forecast 12-month period, each utility applied a different approach to arrive at the reference price of the gas for board approval. This reference price is the Alberta price, or Empress price, discussed earlier in the section on natural gas pricing, which is derived from the New York Mercantile Exchange price. One utility applied a daily exchange rate to arrive at the price in Canadian dollars, while the other utility applied a monthly average exchange rate. These two approaches resulted in one utility establishing a higher Empress base price than the other. For 2013/14, this higher base price had a \$2.8 million impact on the utility's customers, based on their level of gas consumption. According to board staff, this amount would ultimately be adjusted to the actual costs of gas purchased. However, board staff do not review the details of the utilities' gas cost adjustment accounts, which track the differences between forecast and actual purchase prices, to ensure that the appropriate adjustments are being made.

In addition, under the Board's Reporting and Record Keeping Requirements for Gas Utilities Policy, utilities are required to maintain records, which the Board may request to examine, of information supporting the prudence of their gas purchases. These include, for example, a summary of contracts for gas supply and for gas transportation to Ontario, information on available gas storage,

and details to support the monthly gas price adjustment associated with specific purchases occurring in that month. Entries to the cost adjustment accounts are required to include clear and detailed explanations. Management reports must also be maintained, to support purchasing decisions.

We found that board staff did not obtain any of the above source documents to assess the accuracy and validity of the information provided in the applications. Board staff indicated the Board's audit staff monitored compliance with these requirements through separate reviews. Our review of audits conducted by board staff in the past 10 years showed that only one utility was audited for compliance with these requirements, in 2011. This audit identified a number of concerns, including an out-of-period adjusting entry of \$2.6 million related to 2006 that was recorded in 2008, yet the utility had not informed the Board of this out-of-period adjustment. Without sufficiently examining actual purchase records of the two utilities that supply over 99% of the gas consumed in Ontario and that also operate in other provinces, the Board might not have taken sufficient care to protect Ontario consumers from the possibility of inappropriate charges being passed through to them.

RECOMMENDATION 2

To ensure that information submitted to the Ontario Energy Board (Board) by the gas utilities that it regulates is accurate and valid and that consumers are being charged for only the actual costs incurred by utilities to purchase gas, board staff should:

- periodically select source documents from utilities for review, such as contracts, gas purchasing details and management reports, to assess the validity and reasonableness of utilities' application information; and
- periodically review price adjustment accounts and assess the appropriateness of items and entries included in these accounts.

BOARD RESPONSE

The Board accepts this recommendation.

The Board notes that the Audit & Performance Assessment unit is currently undertaking an audit of one of the major gas distributors with respect to that distributor's commodity accounts and related accounting policies, procedures and processes. The audit will include an examination of the distributor's gas price forecasting methodology, its gas purchase and tendering practices and its compliance with board-approved policies, procedures and accounting treatment.

That audit will be completed by the end of the Board's fiscal year. The Board anticipates that comparable audits will be undertaken in respect of the other gas distributors in 2015.

Regulating Gas Marketers

Under the *Ontario Energy Board Act*, gas marketers operate as brokers, locating natural gas on the market to sell competitively. They are licensed to operate to increase competition in the gas sector. Marketers are not subject to board regulation in the rates they charge their customers, but they are required to be licensed to sell gas to low-volume users (annual usage of less than 50,000 m³). Also, the Board does not regulate rates for gas utilities that distribute less than 3 million m³ of gas a year. This would apply to about eight entities that had about 80,000 customers in total as of January 2013, including two municipally operated utilities that are licensed as gas marketers. The *Ontario Energy Board Act, 1998* specifically exempts municipally operated utilities from rate regulation by the Board if they were in operation under the *Public Utilities Act* prior to 1998; this exemption applies to these two utilities. The rates charged by these two municipal utilities are approved by their municipal governments and are not required to be reported to the Board. Similar to the regulated utilities, these municipal utilities also operate as gas distributors.

The Board's processes for issuing and renewing licences was in accordance with their policies. The process took into account factors such as the applicant's prior conduct as an indicator of future conduct with consumers; past and projected financial performance as an indicator of the ability to function economically and efficiently; and technical training and experience as indicators of the ability to understand the energy sector.

Consumers have the option of purchasing their natural gas from gas marketers through fixed-term contracts ranging from one year to five years. Although the gas marketers' rates are not regulated by the Board, starting in 2010 the Board's Reporting and Record Keeping Requirements have required gas marketers to submit information on their contract rates to the Board each quarter. This data has not been published by the Board, which collects it for its own information purposes.

To protect consumers in their decisions to purchase gas from the gas marketers, the legislation requires gas marketers to provide to the potential customer a comparison showing the amount of the customer's current gas bill versus the customer's bill based on the price offered by the marketer. This comparison is made between the gas marketer's fixed-term-contract prices for one to five years and the utility's price, which is the price of the gas supplied for a specific quarter and is adjusted each quarter. Our review of gas contract rates charged by various gas marketers for the quarter ended March 31, 2014, showed that the rates varied significantly among marketers, as seen in **Figure 3**.

Figure 3: Variation in Marketers' Gas Rates, Quarter Ended March 31, 2014

Source of data: OEB

| Contract Terms | Cost per m ³ of Natural Gas (¢) | | % Difference |
|----------------|--|------|--------------|
| | Low | High | |
| One-year | 12.0 | 46.8 | 290 |
| Two-year | 14.4 | 23.1 | 60 |
| Three-year | 14.9 | 39.8 | 167 |

Improvement Needed in Addressing Consumer Complaints

The Board's regulatory responsibilities include responding to inquiries and addressing complaints received from natural gas customers regarding the activities of the regulated gas utilities and licensed gas marketers. Customers can contact the Board via telephone, through the Board's website or in person. Before registering a complaint with board staff, customers are requested to contact the appropriate gas utility or gas marketer. If a customer has contacted the gas utility or gas marketer and is not satisfied with the response or resolution, the complaint is then logged by board staff for follow-up with the gas utility or marketer. We found that it took the Board, on average, about 31 days for utility complaints and 33 days for gas marketer complaints to be addressed. This includes the time from date of receipt of the complaint to board staff review of responses provided by the utilities or gas marketers.

The number of complaints registered against gas marketers declined from 2,774 in 2009 to 539 in 2013, a decrease of 81%. We noted that this decrease in gas marketer complaints followed increased efforts by board staff to ensure gas marketers' compliance with the new requirements of the *Energy Consumer Protection Act* and to educate consumers and communicate consumer protection information through the Board's website. These efforts were effective in reducing the number of complaints. The decrease in complaints also coincided with a fall in the number of consumers buying gas from the marketers.

However, we noted that complaints about contract cancellation and renewal issues were still frequently raised, as consumers often found after signing contracts with marketers that they could pay lower prices with the local utility or with other gas marketers. Providing consumers with rate information from the various natural gas market participants would enable them to make more informed decisions before entering into a contract. Regulatory bodies in Pennsylvania and Ohio provide data on their

websites on the rates charged by their gas marketers along with other consumer protection information.

Since 2010, gas marketers in Ontario have been required to submit to the Board consumer complaints that they receive and address each quarter. We found that board staff did not review this complaint data for trends and patterns or compare it against data on complaints received directly by the Board, in order to identify anomalies for further investigation. We compared the two sources of data and found significant anomalies in a number of complaints received. For example, our review of the complaints received directly by gas marketers for the years 2010 to 2013 found that one gas marketer with about 160,000 customers reported receiving 1,700 complaints, while another gas marketer with about 130,000 customers reported 11,000 complaints—a difference of approximately 9,000 complaints between two similar-sized gas marketers. Our review of complaints received directly by board staff for these same two marketers showed that the Board received a similar number of complaints for each. When we brought this to their attention, board staff indicated that the difference was due to the lack of a board definition for complaints to be reported. This resulted in each gas marketer using a different definition of what constitutes a complaint to be reported to the Board.

RECOMMENDATION 3

To provide consumers with the information they need to make informed decisions in selecting a gas marketer and to protect consumers' interests, and to be in a position to assess consumer complaints regarding gas marketers, the Ontario Energy Board (Board) should:

- consider including on its public website information on the gas rates offered by the various gas marketers for consumers to consult before entering into a contract; and
- define the types of issues to be classified as consumer complaints for reporting purposes, so that the Board can compare the

data on complaints it receives directly from consumers to the data on complaints that gas marketers report to the Board, in order to identify any anomalies and other areas of concern for further follow-up.

BOARD RESPONSE

The Board accepts this recommendation.

The Board has initiated a comprehensive review of the effectiveness of the consumer protection measures in the *Energy Consumer Protection Act*. In connection with that review, the Board will consider the appropriateness and practicality of including on its website information regarding the prices offered by gas marketers.

The Board is also taking steps to clarify the types of issues that should be classified as “consumer complaints” for reporting purposes.

Monitoring Compliance and Enforcement

Board staff have the authority to conduct compliance and inspection audits and reviews of gas marketers and gas utilities to assess their compliance with applicable legislative and regulatory requirements. Staff also have the authority to review compliance with board-established requirements as set out in various documents such as the Gas Distribution Access Rules (which include service quality requirements for utilities), the Code of Conduct for Gas Marketers, and Reporting and Record Keeping Requirements for both. The Board's licensing requirements for gas marketers specifically list compliance requirements.

Two units within the board staff are responsible for conducting these reviews and audits: the Consumer Protection Unit and the Audit and Performance Assessment Unit. Usually, on a weekly basis these two units present identified issues of non-compliance to a Compliance Review Committee to determine the action to be taken. This could include

conducting further work through an audit, inspection or investigation; monitoring future activity; providing guidance to a single licensee or the industry; recommending enforcement action (including seeking an assurance of voluntary compliance or issuing a notice of intention to make an order); or suspension of a licensed activity. The Board also has the option to levy administrative penalties against gas marketers and gas utilities. These administrative penalties vary according to the severity of the impact of non-compliance on consumers and the severity of the deviation from legislative and regulatory requirements. The maximum administrative penalty the Board may impose is \$20,000 for each day or part of a day on which the contravention occurred or continues.

Inspection Efforts Focused Primarily on Gas Marketers

We found that the Board's Consumer Protection Unit, composed of four staff members and a manager, focused its compliance efforts on gas marketers, although in 2012 the marketers sold gas to less than 15% of the gas consumers in Ontario. The gas marketers became the Board's primary focus as a result of numerous consumer complaints prior to the *Energy Consumer Protection Act* in 2011. This Act established consumer protection requirements directed to gas marketers who sold to low-volume consumers (those who consume less than 50,000 m³ annually). **Figure 4** shows the number of inspections conducted since 2009 and the administrative penalties levied.

The Consumer Protection Unit implemented its first risk-based compliance plan in 2013/14 to proactively identify high-risk areas of focus for compliance activities for both the electricity sector and natural gas sector. Before this time, most inspections were conducted in reaction to consumer complaints received. The exception to this occurred in 2011/12, with the introduction of the *Energy Consumer Protection Act*, effective January 1, 2011. Under the *Ontario Energy Board Act*, gas marketers

are required to submit a certificate of compliance with the Act and with applicable regulations and board rules, codes and orders. In 2011/12, board staff contracted with an external consultant to conduct inspections of all gas marketers that had submitted certificates in that year, to determine whether the marketers were in fact complying with all requirements.

The external consultant's work identified issues of non-compliance for all marketers that were inspected. The common types of non-compliance identified were related to identification badge content requirements, completion of price comparisons and disclosure statements, contract content requirements for customer cancellations, gas marketers' handling of complaints, and content of training materials for gas marketer staff. In the majority of cases, the marketers entered into assurances of voluntary compliance and had administrative penalties levied. Subsequent to these reviews the consumer protection unit continued to review these marketers' compliance with the requirements set out in the self-declared certificates of compliance.

Insufficient Audits of Gas Utilities

The Audit and Performance Assessment Unit, composed of four staff and one manager, conducts financial and operational audits of gas utilities. Its activities include assessing whether accounting policies and practices are appropriate to generate reliable data; reviewing specific financial accounts that impact regulatory decision-making; and auditing for compliance to board requirements, such as service quality requirements intended to protect consumer interests. The unit also conducts follow-up audits of previously identified issues.

Two municipal utilities are licensed as gas marketers. Since these municipal utilities are system gas distributors and do not market or enter into contracts with their customers, the Board approved their licences with certain exemptions from both the Code of Conduct for Gas Marketers and its Reporting and Record Keeping Requirements.

Figure 4: Consumer Protection Unit Inspections and Administrative Penalties Levied, 2008/09 to Date

Source of data: OEB

| Fiscal Year Ended | # of Inspections | # of Entities Fined | |
|------------------------|------------------|--------------------------------------|--------------------------|
| | | Administrative Penalties Levied (\$) | Administrative Penalties |
| 2008/09 | 1 | 0 | 0 |
| 2009/10 | 2 | 75,000 | 2 |
| 2010/11 | 4 | 234,000 | 1 |
| 2011/12 | 20 | 967,500 | 12 |
| 2012/13 | 2 | 21,000 | 2 |
| 2013/14 | 20 | 120,000 | 1 |
| 2014/15 as of May 2014 | 2 | 830,000 | 2 |
| Total | 51 | 2,247,500 | 20 |

However, these municipal utilities are still required to meet certain licensing requirements related to these rules. Board staff indicated that they have not conducted any inspection or audit work at either of these municipal utilities to assess their compliance with specific licensing requirements.

For the two rate-regulated gas utilities that supplied more than 99% of the natural gas consumed in Ontario, the Audit and Performance Assessment Unit conducted four gas utility audits and three follow-up audits between 2009/10 and 2012/13. These audits addressed compliance with service quality requirements, one utility's allocation of costs between its regulated and unregulated activities, and one utility's gas cost adjustment accounts, also known as purchase gas variance accounts (PGVAs). These accounts track differences between the forecast and actual purchase costs of gas. The PGVAs are critical for adjusting gas purchase costs and contracts for transportation of gas to Ontario, all of which are pass-through costs that significantly impact consumer rates. Over the last 10 years only the one audit mentioned above was done, in 2011, of PGVAs and processes in accounting for gas costs, and on only one utility. Board staff had not conducted a similar review for the other two regulated utilities since 2000.

The PGVA audit conducted in 2011 identified a number of concerns that are relevant to the utility's

consumer rates. They included the following: the utility not disclosing to the Board an out-of-period adjusting entry of \$2.6 million (as mentioned in the section "Additional Review Needed for Accuracy and Validity of Information Submitted to the Board"), not accruing unbilled gas inventory on a quarterly basis to be consistent with the principles of the quarterly adjustment process, not documenting justification for purchasing gas from suppliers who offered gas prices that were higher than the lowest bid prices, not having a clear policy for competitive purchasing, and not complying with the commitment made to the Board in 2000 to update documentation of the utility's gas cost system procedures (updating commenced nine years later, in 2009, and was under way during the 2011 audit; it was completed by December 2011).

RECOMMENDATION 4

To more effectively oversee the regulated gas utilities in the interest of consumers, and to ensure the validity and accuracy of information they are required to provide to the Ontario Energy Board (Board) to protect the interests of consumers, the Board should conduct more frequent inspections and audits of the regulated utilities that supply more than 99% of the gas consumed in Ontario, especially in areas that

significantly impact consumer rates such as price adjustment accounts, purchasing processes and capital expenditures.

BOARD RESPONSE

The Board accepts this recommendation.

As noted above in the Management Response to Recommendation 2, the Board is currently engaged in an audit of one of the gas distributors and anticipates that further audits will proceed during 2015.

The Board also notes that in 2013, it developed and adopted a risk-based approach to the assessment of compliance by gas and electricity distributors. That risk-based approach assists the Board in focusing its compliance-related resources in an effective manner. That approach is being implemented over the course of the 2014 fiscal year.

Improvement Needed in Assessing Performance of Gas Utilities

A 2010 United Kingdom report on a regulatory agency similar to the Board indicated that the measure of the effectiveness of an organization's performance also relies on an assessment of the performance of its regulated entities. It suggests that it is "common, and good practice, for regulators to use a basket of indicators to judge companies' performance, and to analyze trends in data not just year-on-year performance. This is because annual performance measures, particularly in infrastructure industries, can be strongly influenced by exceptional external events, and can mask underlying problems which may only become apparent in the longer term." We noted that the Board had only a few customer-focused performance measures regarding service quality requirements in place to assess the gas utilities' performance. It had no performance measures for operational effectiveness, financial performance or public-policy

responsiveness, as exist for the electricity sector. In its oversight of Ontario's electricity sector, board staff are in the process of establishing scorecards to enable the Board to assess the electricity market participants' performance annually. Board staff indicated that they will make a determination in the future as to whether these scorecards will be developed for gas utilities.

RECOMMENDATION 5

To more effectively oversee the regulated gas utilities in the interest of consumers, the Ontario Energy Board should establish additional gas-utility-specific performance measures needed to assess utility performance on an ongoing basis and to identify trends over time.

BOARD RESPONSE

The Board accepts this recommendation.

The Board has recently adopted a range of annual reporting requirements for each of the two major gas distributors. These reporting requirements address operations, financial results, service quality performance, capital additions, and gas supply planning. Beginning in 2015, each of the two major gas distributors will review its performance annually with stakeholders and the Board.

The Board will work with the gas distributors to ensure that the annual reporting in respect of existing performance measures is published in a format that is open and accessible to all interested parties and consumers.

Monitoring the Board's Performance

The Ministry of Energy (Ministry) has oversight of the Board and applies a number of tools to enable it to monitor the Board's operations. The Board is required, among other things, to comply with the Agency Establishment and Accountability Directive,

as the Board is a Crown agency; comply with the terms of the memorandum of understanding setting out the responsibilities between the Minister, the Chair of the Board, the Deputy Minister and the Management Committee of the Board; and submit a multi-year business plan and an annual report to the Ministry. According to the *Ontario Energy Board Act, 1998*, the Board is required to submit its annual report to the Ministry within six months after the end of its fiscal year; then, within one month after receiving the annual report, the Minister of Energy must table the report before the Legislative Assembly. Once the tabling requirements are met, the Board is required by the memorandum of understanding to publish the annual report on its public website. We found that although the Board filed its 2011/12 and 2012/13 annual reports within the required time periods, the Minister did not table the reports within one month of receipt in the Legislative Assembly as required by law, and therefore the reports were not posted on the Board's website until April 2014.

The Board's multi-year business plan sets out its strategic direction and covers a three-year period. The 2012 and 2013 business plans listed four high-level visions of the outcomes to be achieved in the energy sector over a five-year period, and the management initiatives required to meet them. The business plans state that:

- Through the Board's regulatory framework, distributors, transmitters and other regulated entities will invest and operate in a manner that increases efficiency and productivity and provides consumers with a reliable energy supply at a reasonable cost.
- The Board's own processes will be efficient and cost-effective and will be understood by and accessible to industry and consumers.

The business plans list strategic initiatives that are intended to move the Board toward its high-level outcomes. At the time of our audit, board staff indicated that, as one such initiative, they would be commencing a review of the effectiveness of the Low-Income Energy Assistance Program, which

provides financial assistance to families whose incomes fall below a certain limit.

The Board's annual report shows each initiative as listed in the multi-year plan and the Board's progress in achieving each one. The results are audited annually by an external party. These results serve two purposes: they assess the Board's achievement of its objectives, and they are linked to the annual incentive payments made to both union and non-union staff. A minimum rating of 70% must be achieved for annual incentive payments to be paid each year. We noted that the management committee of the Board, based on certain criteria, can adjust targets throughout the year if certain initiatives are not progressing as expected due to, for example, changed priorities, replacement with new initiatives or the decision that the initiatives are no longer required. For the 2011/12 and 2012/13 years, the Board's completion rating was assessed at over 95%.

Our 2011 audit of electricity regulation noted that board performance measures were not based on outcomes. In its 2011–14 business plan the Board indicated that it will continue to rely on current measures of performance while it develops a performance-assessment framework that it can use to assess whether the desired outcomes of its decisions and policy initiatives have been achieved. In December 2011, the Board released a Policy Evaluation Framework to allow it to monitor and evaluate the effectiveness of its policies. The Board had not yet used the evaluation framework to evaluate the effectiveness of any of its policies.

Lack of Assessment of the Board's Performance in Meeting Its Mandated Objectives

The *Ontario Energy Board Act* establishes among the Board's objectives the protection of consumers' interests and facilitation of competition in the sale of gas to users. These objectives, however, are to be accomplished in the context of a number of structural hurdles in the province's energy sector.

The allocation of service territories to utilities for delivery of gas has a significant impact on competition. Since the 1990s and the introduction of retail competition in gas markets, gas distributors no longer have a monopoly on the supply of natural gas. Service territories have been historically allocated to utilities through board-granted Certificates of Public Convenience and Necessity, and by municipal franchise agreements that give utilities the right to operate and maintain infrastructure and distribute gas within municipalities. Some territories have had their gas provided by a particular utility since as far back as the 1850s. These agreements have been continually renewed with the same providers or with providers who amalgamated with the previously existing providers. In 2011, the most recent year for which data is available, about 400 utility-municipality agreements existed across the province. Board documentation indicates that very few municipalities change their natural gas provider once these agreements are signed, mainly because they lack an alternative pipeline infrastructure.

With the deregulation of the natural gas sector in the mid-1980s, the Board implemented a number of policies to facilitate competition. These included policies that required utilities to pass through to customers the gas costs paid with no profit component, and policies that allowed marketers to sell natural gas under fixed-term contracts ranging from one to five years, while requiring utilities to be default suppliers so they cannot enter into fixed-term contracts with customers. The purpose of these policies was to give customers flexibility to change their gas provider at any time. However, an assessment has not been done of the effectiveness of these policies in facilitating competition in the sale of gas.

In addition to these two objectives, the Board has the following mandated objectives under the *Ontario Energy Board Act, 1998 (Act)*:

- to facilitate rational expansion of transmission and distribution systems;
- to facilitate rational development and safe operation of gas storage;

- 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;
- to facilitate the maintenance of a financially viable gas industry for the transmission, distribution and storage of gas; and
- to promote communication within the gas industry and the education of consumers.

The Act also requires the Minister of Energy to have a report prepared every five years on the Board's effectiveness in meeting its mandated objectives for tabling in the Legislative Assembly. However, no reviews of the Board's effectiveness have been conducted.

In December 2013, the Minister of Energy requested the Board to complete a review of its effectiveness relating to consumer protection measures under the *Energy Consumer Protection Act, 2010*, and to make recommendations. The Board commenced this review in February 2014.

RECOMMENDATION 6

To determine whether the Ontario Energy Board (Board) is achieving its mandated objectives, the Board should use available evaluation tools, including its Policy Evaluation Framework, and work with the Ministry of Energy to assess the effectiveness of its policies and initiatives in achieving desired outcomes and mandated objectives, including protection of consumer interests and facilitating competition in the sale of natural gas.

In addition, the Minister should table the Board's annual report within one month of receiving it, as required by law.

BOARD RESPONSE

The Board accepts this recommendation.

The Board remains committed to assessing its own performance and the effectiveness of the regulatory policies that it implements.

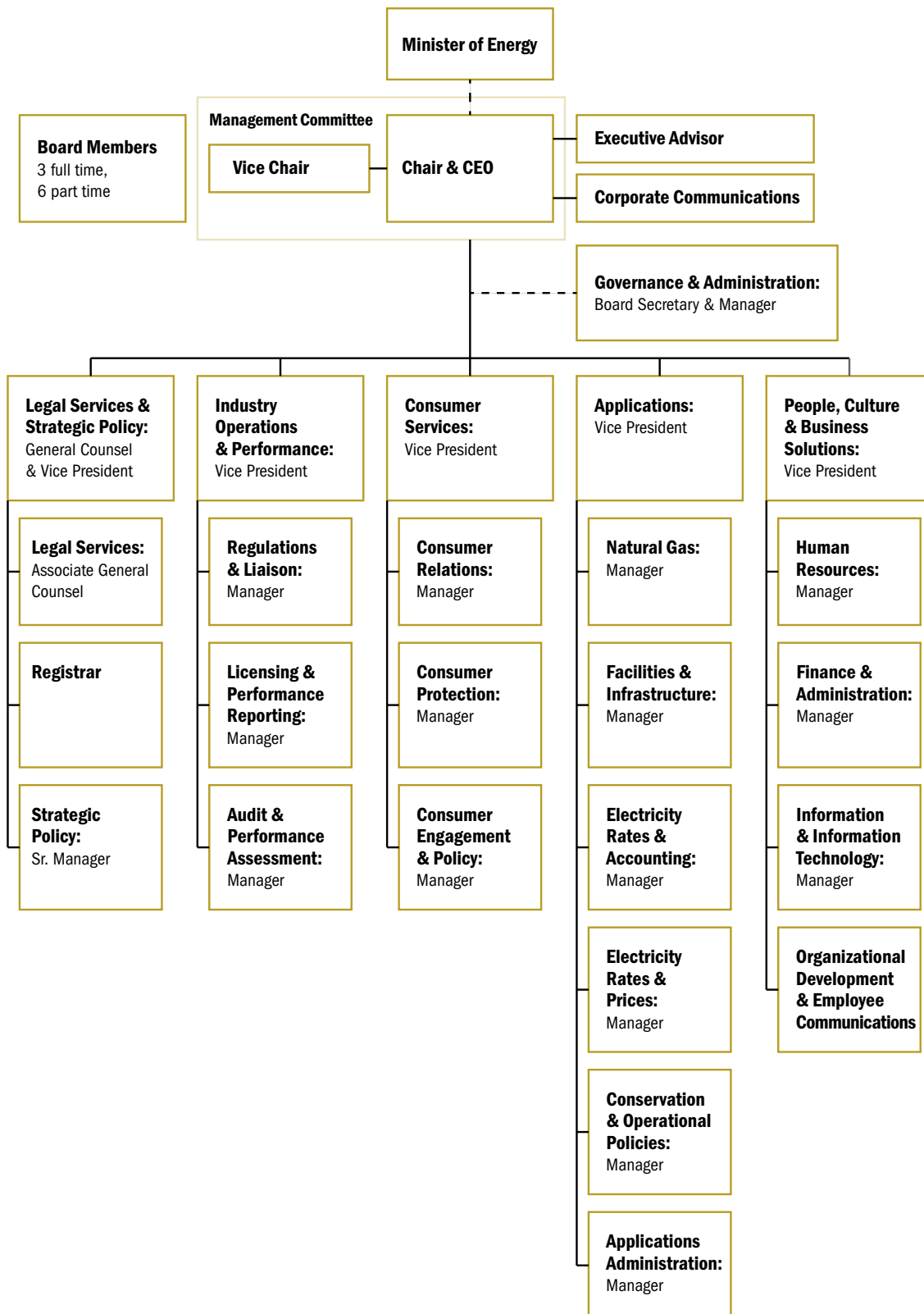
The Policy Evaluation Framework (PEF) adopted by the Board in 2011 distinguished between the evaluation of policy initiatives against short- and medium-term objectives (less than three years) and long-term objectives (greater than three years). The two key policy initiatives implemented at the Board since the adoption of the PEF are the consumer protection measures under the *Energy Consumer Protection Act* (ECPA) and the Renewed Regulatory Framework for Electricity (RRFE).

The Board is currently undertaking a review of the effectiveness of the consumer protection measures under the ECPA. The evaluation framework for the RRFE, which was first applied to electricity distributors in respect of the 2014 rate year, will be established during the 2015/16 fiscal year.

The Board will work with the Ministry with respect to any review of the Board's effectiveness which may be initiated under section 128.1 of the *Ontario Energy Board Act*.

Appendix—Ontario Energy Board Organization Chart*

Prepared by the Office of the Auditor General of Ontario



* There are about 160 total staff.

Glossary of Terms

Prepared by the Office of the Auditor General of Ontario

Cost of service application—Application submitted by gas utilities approximately every five years to establish the base rate to charge customers. Includes information on corporate assets and capital; sales and revenue forecasts; weather forecasts; estimated costs; capital structure; etc. The goal is to determine the revenue requirement (the amount the regulated utility may earn), which is then allocated to be recovered from customers.

Gas marketer—Operates as a broker, locating natural gas to sell competitively, which means that it charges unregulated consumer rates.

Gas utility—Owns the pipes and equipment that deliver natural gas to a home or business. Each utility serves different territories across the province, including municipalities. Its consumer rates are regulated by the Board.

Intervenor—Individual or group representing residential, institutional, commercial and large industrial consumers of energy, and environmental and policy advocacy groups. Intervenors participate in Board proceedings, submitting arguments or written questions, or cross-examining witnesses.

Purchase gas variance account—A utility's gas cost adjustment account that records the differences between the forecast and actual purchase cost of gas by the utility.

Quarterly rate adjustment mechanism—Quarterly adjustment of the rates the utilities may charge their customers for their gas supply. The adjusted rates come into effect each January 1, April 1, July 1 and October 1. The intention is to more accurately reflect market prices, provide price transparency, smooth out large adjustments on customers' bills, and provide fairness and equity in billing.

Rate application process—A process involving several steps from receipt of the gas utility's application for a change in the rate it charges its customers to the Board decision and issuance of the rate order.

Rate regulation—Gas utilities' rates, but not gas marketers' rates, are regulated by the Board. The *Ontario Energy Board Act*, section 36, states:

- No gas transmitter, gas distributor or storage company shall sell gas or charge for the transmission, distribution or storage of gas except in accordance with an order of the Board.

Under Regulation 161/99, section (3):

- Section 36 of the Act does not apply to the sale, transmission, distribution or storage of gas by a distributor who distributes less than 3,000,000 cubic metres of gas annually.

Regulatory hearing—A quasi-judicial process, either oral or written, where a panel of Board members makes decisions regulating the natural gas sector. Hearings are open to the public and broadcast on the Internet.

Revenue requirement—The amount a regulated utility is permitted to earn.