

Blakes Bulletin

Energy—Regulatory

Ontario Energy Board Can Depart From Traditional Rate Making Principles

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On May 16, 2008, the Ontario Divisional Court issued a decision which should be of great interest to companies involved in the distribution of natural gas and electricity who must obtain regulatory approval for their distribution rates.

The court held that the Ontario Energy Board (the OEB) does have the authority to set lower rates for the distribution of natural gas to low income consumers even though such a program would necessarily result in higher prices for the majority of residential consumers, and even though it would be a departure from the traditional model of rate making based on cost causality and cost of service.

Although the case related specifically to the Ontario Energy Board's jurisdiction to set gas distribution rates, the court's findings would likely apply equally to the Board's jurisdiction to set electricity distribution and transmission rates in Ontario.

The case was brought on behalf of the Low Income Energy Network (LIEN). It started in August 2006 when Enbridge Gas Distribution (EGD) filed an application with the Board requesting a rate increase. LIEN proposed that the Board accept as an issue in the rates proceeding the following matter:

Should the residential rate schedules for EGD include a rate affordability assistance program for low-income consumers? If so, how should a program be funded? How should eligibility criteria be determined? How should levels of assistance be determined?

Several parties opposed the inclusion of the issue on the basis that the Board lacked jurisdiction to establish special rates for low income consumers.

In April 2007, the Board issued a split decision in which two out of three panel members held that the Board does not have the jurisdiction to establish rates based on rate affordability for low income consumers.

LIEN appealed to the Ontario Divisional Court. The Divisional Court decision was also a split decision, with two of the three judges reversing the Board's decision and ruling that the Board does indeed have the jurisdiction to establish a rate affordability assistance program. The court, however, made it clear that even though the Board has the discretion to implement rates that favour low income consumers, the Board can refuse to establish such special rate classes when it exercises its discretion.

The Board's jurisdiction to fix rates for the distribution of natural gas in Ontario is found in section 36 of the *Ontario Energy Board Act, 1998* (the Act). Subsection 36(2) of the Act gives the Board the authority to fix "just and reasonable" rates for the distribution and transmission of natural gas, and subsection 36(3) of the Act states that in approving or fixing just and reasonable rates the Board may adopt "any method or technique that it considers appropriate".

The court referred to the fact that the Board has traditionally set rates on a "cost of service" basis, that is, on the basis of cost causality and employing an approach which looks to the utility's capital investments and maintenance costs including a fair rate of return to determine revenues required, with the revenue requirement then being divided amongst the utility's rate paying consumers on a rate class basis (i.e., residential, commercial, industrial, etc.). Rates have been traditionally designed with the principled objective of having each rate class pay for the actual costs that class imposes upon the utility.

The previous legislation had required that the Board use the traditional cost of service analysis to determine rates, but that requirement was repealed when s. 36 of the current Act was enacted.

The court found that the Board could use the traditional cost causality approach to fix rates, but that "the Board need not stop there". It held that the Board is authorized to employ "any method or technique that it considers appropriate" to fix "just and reasonable rates" within the context of the Board's statutory defined objectives set forth in the Act.

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One of the Board's statutory objectives is protecting the interest of consumers with respect to prices. In this case, the objective of protecting "the interests of consumers" could mean taking into account income levels in pricing to achieve the delivery of affordable energy to low income consumers.

The Board's jurisdiction to fix rates for the distribution and transmission of electricity is set out in s. 78 of the Act in exactly the same terms as are used in s. 36 of the Act in respect of the Board's jurisdiction to set distribution and transmission rates for natural gas. Accordingly, electricity distribution companies may well find themselves facing similar arguments in the future from consumer advocacy groups seeking to obtain lower distribution rates for certain classes of low income or disadvantaged customers.

More generally, the LIEN decision is an important precedent for any party who may be seeking to have distribution or transmission rates set on a basis other than by the traditional method based on cost causality and cost of service. It may well be that in practice the Ontario Energy Board will exercise its discretion to depart from standard rate making principles only in exceptional circumstances, but the Divisional Court's decision does establish that the Board has the jurisdiction to do so in appropriate circumstances, and those circumstances need not be limited to implementing rate relief for disadvantaged consumers.

The Board has several statutory objectives other than the protection of the interests of consumers with respect to prices, such as to facilitate the maintenance of a financially viable electricity industry and a financially viable gas industry for the transmission and distribution of gas, and it can be argued based on the LIEN decision that the Board has jurisdiction to depart from standard rate making principles in order to promote another of those objectives.

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