

Ontario Energy Board
P.O. Box 2319
2300 Yonge Street
27th Floor
Toronto ON M4P 1E4
Telephone: 416-481-1967
Facsimile: 416-440-7656
Toll free: 1-888-632-6273

Commission de l'énergie de l'Ontario
C.P. 2319
2300, rue Yonge
27^e étage
Toronto ON M4P 1E4
Téléphone: 416-481-1967
Télécopieur: 416-440-7656
Numéro sans frais: 1-888-632-6273



COMPLIANCE BULLETIN

DATE ISSUED: July 7, 2010

**TO: All Licensed Electricity Distributors
All Other Interested Parties**

RE: Distributor-Owned Generation: Application of Section 71(3) of the *Ontario Energy Board Act, 1998*

This Bulletin provides guidance in relation to a number of issues associated with the application of section 71(3) of the *Ontario Energy Board Act, 1998* regarding the ownership and operation of generation and energy storage facilities by electricity distributors.

1. Background

Under section 71(3) of the *Ontario Energy Board Act, 1998* (the "OEB Act"), added by the *Green Energy and Green Economy Act, 2009*, electricity distributors may now own and operate certain generation and energy storage facilities ("qualifying facilities").

Prior to this amendment, electricity distributors were precluded by section 71(1) of the OEB Act from engaging in the ownership and operation of qualifying facilities (among others) as a business activity. The *Green Energy and Green Economy Act, 2009* also

added the following new objective to guide the Board: “to promote the use and generation of electricity from renewable energy sources in a manner consistent with the policies of the Government of Ontario...”

As stated in the Board’s “Guidelines: Regulatory and Accounting Treatments for Distributor-owned Generation Facilities” (G-2009-0300), the ownership and operation of qualifying facilities is not currently a rate-regulated activity under section 78(3) of the OEB Act. Qualifying facilities are not included in rate base and any costs in respect of such facilities are not recovered through rates.

Board staff has received a number of inquiries relating to section 71(3) of the OEB Act and has identified several issues relating to that section in respect of which staff believes that further guidance would be of assistance to the industry. This Bulletin sets out Board staff’s views on five issues pertaining to the application of section 71(3) of the OEB Act.

For convenience of reference, section 71 of the OEB Act is reproduced in its entirety in Appendix A.

2. Application of Section 71(3) of the OEB Act

1. *What does “own” mean in the context of section 71(3) of the OEB Act?*

The OEB Act does not contain a definition of the term “own” or of the term “ownership” for the purposes of section 71(3) or for any other purpose.

In Board staff’s view, section 71(3) of the OEB Act clearly allows qualifying facilities to be owned directly by the distributor. The question arises whether any arrangement other than this most straightforward direct ownership structure may also qualify as ownership of a qualifying facility within the meaning of section 71(3) of the OEB Act.

Board staff's view is that section 71(3) should not be interpreted as precluding all ownership structures or ownership interests that fall short of 100 per cent direct ownership of the qualifying facility as an asset of the distributor. An appropriate interpretation needs to reflect the Board's objective of promoting the use and generation of electricity from renewable resources, while also reflecting the Board's other objectives.

In Board staff's view, an appropriate approach to the concept of ownership in the context of section 71(3) of the OEB Act is one that facilitates distributor participation in the development of qualifying facilities while protecting the interests of consumers by minimizing the risk that these activities will have an adverse effect on a distributor's financial position. Accordingly, Board staff's view is that, in order to "own" a qualifying facility within the meaning of section 71(3) of the OEB Act, a distributor must have a controlling interest in the entity that owns the qualifying facility. Where that entity is a corporation, Board staff believes that a distributor will have a controlling interest if it: (i) holds voting shares carrying more than 50% of the votes for the election of directors; and (ii) the votes carried by such shares are sufficient to elect a majority of the board of directors. This is consistent with the concept of "control" as used in the *Business Corporations Act* (Ontario). In the case of other forms of business organizations (such as partnerships), Board staff believes that a distributor may have a controlling interest if the distributor is able to demonstrate that it controls the management and key decision-making in respect of that organization.

All subsequent references in this Bulletin to "own" or "ownership" should be read in a manner consistent with the above.

2. *Does section 71(3) of the OEB Act require a distributor to both own and operate a qualifying facility? Can a distributor own but not operate a qualifying facility or operate a qualifying facility that it does not own?*

Board staff's view is that section 71(3) of the OEB Act was intended to contribute to the development of generation from renewable sources by providing an opportunity for additional participants (notably, electricity distributors) to develop new renewable generation facilities.

In Board staff's view, it is clear that a distributor that owns a qualifying facility may, as a related activity, operate that qualifying facility. Board staff does not believe that section 71(3) of the OEB Act precludes a distributor from contracting out the operation of a qualifying facility that it owns, provided that the distributor ultimately remains responsible and accountable to the Board for all applicable legal and regulatory requirements relating to the operation of the qualifying facility. Distributors regularly contract out portions of their system operation functions, and Board staff does not believe that it would be in keeping with the Board's objective of promoting renewable generation to read into section 71(3) of the OEB Act a prohibition against the contracting out of qualifying facility operations.

Section 71(3) of the OEB Act empowers distributors to "own *and* operate" qualifying facilities, and does so as an exception to the general prohibition in section 71(1) against non-distribution business activities. In Board staff's view, section 71(3) was not intended to allow electricity distributors to assume the role of simply acting as a service provider (operator) to third party generation proponents. Had that been the intention, Board staff believes that section 71(3) would have authorized distributors to "own *or* operate" qualifying facilities. Accordingly, in Board staff's view, section 71(3) does not permit a distributor to engage in the business of operating qualifying facilities, or any other generation or energy storage facilities, that it does not own.

3. *Does section 71(3) of the OEB Act restrict a distributor to owning and operating only one qualifying facility?*

Section 71(3) of the OEB Act states that a distributor may own and operate “a” qualifying facility or “an” energy storage facility. A strict and literal approach to the application of this section would limit each distributor to the ownership and operation of only one qualifying facility. However, in Board staff’s view, it is appropriate to take a more purposive approach to the application of section 71(3) of the OEB Act that recognizes and reflects the Government’s policy goals as expressed in the Board’s objective of promoting the use and generation of electricity from renewable energy sources. In that context, and in the context of a diverse distribution sector that includes large distributors that have the potential to contribute significantly to the achievement of the Government’s renewable energy policy goals, Board staff’s view is that section 71(3) of the OEB Act should not be applied in a manner that limits the number of qualifying facilities that a distributor may own and operate.

Board staff believes that this more purposive approach is consistent with the terms of Order in Council No. 1540/2009 dated September 8, 2009, and with the Minister’s Directive to the Board that was approved by that Order in Council. These documents permit Ontario’s two largest gas utilities to own and operate qualifying facilities. The Order in Council states that it is desirable for these gas utilities to be “accorded authority similar to those of electricity distributors” under section 71(3) of the OEB Act. The Minister’s Directive, in turn, refers to the facilities that may be owned and operated by the gas utilities in the plural: “...the ownership and operation of: (a) renewable energy electricity generation facilities each of which does not exceed 10 megawatts...; (b) generation facilities that use technology...; (c) energy storage facilities which meet the criteria...”.

Board staff reminds distributors that each qualifying facility must, in all respects, meet all prescribed criteria. For example, a renewable energy generation facility may not exceed 10 megawatts or such other capacity as may be prescribed by regulation.

4. *May a distributor own and operate a qualifying facility that is located outside its licensed service area?*

Board staff notes that section 71(3) of the OEB Act does not expressly speak to this issue. Staff also notes that the ownership and operation of a qualifying facility is an activity separate and distinct from the business of distributing electricity that is covered by a distribution licence and constrained to a specific service area.

Therefore, Board staff's view is that there is no statutory prohibition against a distributor owning and operating a qualifying facility outside of the distributor's licensed distribution service area. Board staff reminds distributors that, subject to any exemptions set out in regulations under the OEB Act, a licence is required to generate electricity or ancillary services for sale.

5. *Does section 80 of the OEB Act apply to the ownership of generation facilities that are qualifying facilities?*

Under section 80 of the OEB Act, a distributor is required to give notice to the Board of any proposal to "acquire an interest in a generation facility in Ontario, construct a generation facility in Ontario or purchase shares of a corporation that owns a generation facility in Ontario". Board staff notes that there is nothing in the OEB Act or the regulations made under that Act that would exempt a distributor from the requirement to give notice under section 80 in respect of a proposal to acquire ownership of a generation facility that is a qualifying facility. Revisions to the Board's "Preliminary Filing Requirements for a Notice of Proposal under Sections 80 and 81 of the *Ontario Energy Board Act, 1998*" are being developed and will be issued in the near future.

In Board staff's view, the authority of distributors to own and operate generation facilities is found in section 71(3) of the OEB Act and is limited by the scope of that section. In that regard, Board staff's view is that section 80 of the OEB Act does not create any

additional right or authority, over and above that found in section 71(3), regarding the ownership and operation of generation facilities.

The views expressed in this Bulletin are those of Board staff and are not binding on the Board.

Any enquiries regarding this Bulletin should be directed to the Board's Market Operations hotline, at 416-440-7604 or market.operations@oeb.gov.on.ca.

Yours truly,

Original Signed By

Aleck Dadson
Chief Operating Officer
Ontario Energy Board

APPENDIX A

Section 71 of the *Ontario Energy Board Act, 1998*

Restriction on business activity

71. (1) Subject to subsection 70 (9) and subsection (2) of this section, a transmitter or distributor shall not, except through one or more affiliates, carry on any business activity other than transmitting or distributing electricity.

(2) Subject to section 80 and such rules as may be prescribed by the regulations, a transmitter or distributor may provide services in accordance with section 29.1 of the *Electricity Act, 1998* that would assist the Government of Ontario in achieving its goals in electricity conservation, including services related to,

- (a) the promotion of electricity conservation and the efficient use of electricity;
- (b) electricity load management; or
- (c) the promotion of cleaner energy sources, including alternative energy sources and renewable energy sources.

(3) Despite subsection (1), a distributor may own and operate,

- (a) a renewable energy generation facility that does not exceed 10 megawatts or such other capacity as may be prescribed by regulation and meets the criteria prescribed by regulation;
- (b) a generation facility that uses technology that produces power and thermal energy from a single source that meets the criteria prescribed by regulation; or
- (c) an energy storage facility that meets the criteria prescribed by regulation.