

Model Franchise Agreement Review



RATIONALE

The Ontario Energy Board's Model Franchise Agreement governs the relationship between municipalities and utilities. Given that Ontario is developing a Framework for Energy Innovation: Distributed Energy Resources and Utility Incentives and updating its Long-Term Energy Plan, now is an ideal time to ensure a level playing field principle is advanced via the update to the Model Franchise Agreement. An amendment to Regulation 584 in the Ontario Municipal Act is a prerequisite of such a change.

The goal of this letter is to engage with the Province of Ontario to ensure a transparent and equitable framework across different users by including a provision for municipal access fees to be paid to municipalities for use of their right of way for natural gas distribution infrastructure and other associated pipelines that use the municipal right of way.

Many municipalities in Ontario are experiencing unprecedented growth within their communities. The City of Ottawa is projected to increase in population by almost 50% in the coming 30 years. This results in significant pressures on municipalities to manage the growth and advance complete communities that address environmental, social, and economic outcomes.

There has been increased demand regarding access to the municipal right of way, from the municipalities' own infrastructure (sewer, stormwater, water supply), but also from utilities (electrical and natural gas), as well as telecommunications. Increasing opportunities to meet local energy needs with local energy solutions are also likely to place additional pressures on right of way infrastructure.

The City of Ottawa is requesting a review of the arrangements between municipalities and utilities, especially natural gas utilities. They are private entities which use the municipal right of way without accounting financially for the costs borne by the municipality and lost opportunities related to increased demand and limited space in the municipal right of way. This, thereby, results in a subsidy to the fossil fuel sector.

Municipalities across Ontario are developing Community Energy and Emissions Plans^[1] to stimulate local economies by keeping energy dollars local, and to meet net zero emissions targets. The City of Ottawa's plan, the Energy Evolution Strategy, aligns with International, Federal, and Provincial GHG reduction targets. It also aligns with the stated goals in the Province's Made in Ontario Climate Plan which looks to "support the clean technology sector as part of our broader economic growth and recovery efforts."^[2]

Currently, gas utilities in Ontario pay neither access fees nor payments in lieu of taxes to municipalities. For comparison, municipally-owned utilities pay significant dividends to the municipality, and private electric utilities pay taxes on use of right of way lands as regulated under Ontario Regulation 387/98^[3]. That regulation does not authorize municipalities to charge taxes for access to right of way lands to gas utilities.

Most provinces in Canada allow municipalities to charge utilities (including natural gas utilities) for access to public lands for their infrastructure. For example, in Edmonton the gas utility pays 32.9% of delivery charge revenues to the municipality as an access fee for using the municipal right of way. If the Edmonton approach were applied in a city of one million residents, the annual compensation would be approximately \$66 million. We encourage the Ministry of Energy to review any legislation that may be preventing municipalities from charging users such as natural gas distributors for infrastructure encroachments under the City's right of way. Imposing such charges on conventional natural gas distributors will help level the playing field between entities that use the municipal right of way and between fossil fuels and low carbon energy systems that are seeking access to municipal rights of way.

Space in the public right of way is at a premium to support intensification, in particular underground space. As a result, it is in the public interest to protect underground space in the rights of way through market pricing mechanisms.

Gas infrastructure is the largest private user of underground space because it is typically located underground and requires setbacks from other services for safety, while telecom and electric infrastructure is often run overhead. Any private equipment in the right of way results in additional time and expense to municipalities.

In order to meet GHG reduction targets, municipalities are facing the need to install district energy systems in dense urban areas. To meet public demands for fast internet, fiber optic cables are also adding to pressure in the right of way. In older parts of many municipalities, separation of storm and sanitary sewers or combined sewage storage tunnels is another right of way demand pressure along with the desire to bury overhead electrical distribution. As telecommunications are under federal jurisdiction, municipalities are collectively engaging with the federal government on the telecommunications sector's use of the right of way.

The natural gas utility, as a regulated utility, earns a fixed 9% return on investment through rates based on their infrastructure assets. This means they are incented to expand their gas grid wherever possible. As the Community Energy and Emissions Plans are achieved, it is predicted that the gas grid infrastructure will be increasingly expensive to maintain, leading to increased abandonment by the utility, as allowed under the Model Franchise Agreement. Increased applications for abandonment of natural gas infrastructure in the municipal right of way have occurred and are concerning considering the increased demand on the municipal right of way and future liability this transfers to municipalities.

Municipal costs to implement the Community Energy and Emissions Plans are in the billions; however, they project a net financial gain to Ontario ratepayers by 2050 due to reduced utility bills. Funding for these strategies is limited, given that municipalities do not have powers to advance carbon pricing.

Municipalities are uniquely positioned to offer programs to reduce energy consumption of buildings through municipal mechanisms such as Local Improvement Charges and Community Improvement Plans. Such programs protect ratepayers from energy and carbon cost increases. Also, tenant residents are not engaged by utility conservation programs because they are not incented to improve their rental home. Municipalities can provide programs to support these residents to reduce their exposure to utility bill increases.

FRANCHISE AGREEMENTS IN ONTARIO

In Ontario, 340 municipalities have currently adopted the Model Franchise Agreement as provided by the Ontario Energy Board. Although municipalities theoretically have the ability to negotiate different terms with the natural gas utility, all such requests historically have been denied by the Ontario Energy Board.

These agreements are signed for 20 years, which is longer than the timeframe remaining to meet emissions reduction targets. However, adjustments to the Model Franchise Agreement triggers an adjustment to those that are in place at certain intervals. The Model Franchise Agreement currently in place was last reviewed in 1999. The review prior to that was 1987. Since much has changed since 1999, another review of the agreement is recommended.

The current Model Franchise Agreement allows municipalities to recover expenses related to the natural gas infrastructure in municipal rights of way, but does not include any payment in lieu of taxes, franchise fees, access fees, or land rental fees. The Model Franchise Agreement includes a provision in section 101 that allows natural gas utilities to abandon old equipment in the right of way without being required to remove it. This equates to a subsidy for the gas utilities. For comparison, telecommunications utilities, which are regulated under the federal Telecommunications Act, are required to cover the cost of old equipment removal.

Natural gas contributed 35 MTCO_{2e} of GHGs in Ontario in 2020^[4]. Currently, the private natural gas utilities in Ontario are granted free access to public land for their gas infrastructure^[5]. This equates to a subsidy for the natural gas utility, increased costs on municipalities regarding right of way management and lost potential municipal revenues. This recommendation is in line with the 2009 commitment by the federal government to phase out fossil fuel subsidies by 2025^[6].

JURISDICTIONAL SCAN

Fees are structured slightly differently in various provinces, with authorities bridged between the Provinces and Municipalities in most cases. A scan of the largest cities in Canada provides some insight into the various approaches applied across Canada.

British Columbia

Pursuant to section 23(1)(g) of the Utilities Commission Act (UCA), municipalities can elect to charge an operating fee of their choice, subject to approval by Utilities Commission. This is provided for in the Municipal Act. To date, Surrey is the only Lower Mainland municipality to implement an operating fee, while many on Vancouver Island and the rest of mainland BC have implemented an operating fee. For example, Kelowna, Highlands, Nanaimo, and Nelson, all charge operating fees of 3% of all gas revenues.

Alberta - Edmonton

The Alberta Municipal Government Act enables municipalities to enter into access agreements, or franchise agreements, with utilities, in return for exclusive rights to provide a service within the municipality. It allows municipalities to set the fees based on what they believe to be fair. The fees compensate the City for direct costs, restrictions on planning and development due to utility rights of way, as well as inherent risks related to utility access. Access fees and the basis for calculating them differ for municipalities across Alberta.

Edmonton has been charging gas utilities access fees since 1915. They currently charge the natural gas utility an access fee of 32.9% of delivery revenues. Up to 35% was approved by the Alberta Utilities Commission. The maximum 35% rate is consistent with a template developed collaboratively by the gas utility companies and the Alberta Urban Municipalities Association in 2003.

The annual revenues generated by all access fees in Edmonton represent about 5.3% of the City's annual consolidated operating revenues, a rate that has remained stable over the past 5 years. Natural gas utilities contribute about half of Edmonton's access fee revenues, or \$60.3 million annually^[7] (population 981,280, or \$61/capita).

Saskatchewan – Regina

In 2019 in Saskatchewan, the SaskEnergy Act was amended to give all urban municipalities authority to implement a 5% access fee, also called a surcharge, to gas utilities. The municipal surcharge was put in place to compensate urban municipalities for giving up the right to establish their own natural gas or power distribution systems^[8]. Regina opted to implement this fee in 2019 and now earns \$5.6 million annually (population of 228,928 or \$24/capita).

Manitoba – Winnipeg

Winnipeg has a Charter that authorizes them to implement sales taxes. In 1973, they passed a municipal bylaw to implement sales taxes on natural gas and electricity sales^[9]. The rates for these taxes are 2.5% for domestic purposes and 5% for other than domestic purposes. In 2019, they totaled \$22 million annually in revenues for the City (population 749,534 or \$29/capita).

Nova Scotia – Halifax

Halifax receives an access fee from natural gas utilities who install gas distribution infrastructure in the public right of Way. There is limited natural gas infrastructure in the rest of Nova Scotia, so this provision has limited application elsewhere in the province. The access fee charged by Halifax is equivalent to approximately 2% of the total natural gas bill.

GENERAL REVIEW FOR ONTARIO

An amendment to Regulation 584/06(9) in the Ontario Municipal Act is a prerequisite of the addition of franchise fees in the Model Franchise Agreement. The City of Ottawa supports an amendment to the Regulation 584/06(9) under the Ontario Municipal Act to remove the exemption of gas and electric utilities from municipal access or franchise fees. Such an amendment would require a request to the Minister of Municipal Affairs and Housing to implement the change.

Subsequent to the Regulation amendment, the City then requests a review of the Model Franchise Agreement. The City Council of Ottawa endorsed staff in October 2020 to pursue the right to charge access fees to natural gas utilities for accessing the public right of way. An adjustment to the Model Franchise Agreement would be needed to implement that.

Based on the jurisdictional scan, it appears that an access fee of 5% of gas revenues would be in line with other jurisdictions. This would equate to approximately \$27 per person per year, which is in line with other Canadian municipalities. Revenues would be used for municipal conservation programs that target vulnerable residents and businesses.

To implement changes to the Model Franchise Agreement, the Province would direct the Ontario Energy Board to review the Model Franchise Agreement. Including an access fee equating to 10% of commodity charges, which is approximately equivalent to 5% of gas revenues, would bring Ontario into alignment with other provinces. Applying this charge only to the commodity side would encourage conservation and enable consumer choice.

The City of Ottawa suggests this fee is justified on the basis that municipalities are encumbered and exposed to risk by gas distribution infrastructure in their right of way. Also, municipalities are at the forefront of delivering energy and emissions reduction programs for populations that are not benefiting from utility demand side management programs.

An amendment to section 101 to remove the ability for gas utilities to abandon old equipment in the right of way is also suggested. As demand for space in the right of way increases, these abandoned gas lines will increasingly be a burden on necessary public services.

KEY MESSAGING: ENDING THE MUNICIPAL RIGHT-OF-WAY SUBSIDY FOR FOSSIL FUELS

- » Gas companies in Ontario do not pay municipalities for the right to use an underground network of pipes to deliver gas to customers.
- » In provinces like Alberta, Saskatchewan, and Nova Scotia, municipalities charge an access fee that has raised tens of millions for these communities (e.g., Edmonton, Halifax, Surrey, Kelowna, Regina and Winnipeg). The fees range from a 2% charge in Halifax to 32.9% in Edmonton. Based on Edmonton's rate, Ottawa is being forced to forego \$66M/yr in new revenue, while Toronto is foregoing approximately \$200M.
- » For Ontario municipalities to gain the authority to charge a right-of-way fee for gas, an amendment to the Ontario Energy Board's Model Franchise Agreement is required (through Regulation 584 of the Ontario Municipal Act and a corresponding change to the City of Toronto Act regulations). The Agreement is in the process of being updated.
- » Municipalities are under pressure to manage growing populations while ensuring good environmental, social and economic results. Moreover, underground space for gas pipes is needed by other infrastructure, such as stormwater and sewage infrastructure upgrades, fiber optic cables for high-speed Internet, and buried electrical infrastructure to protect it from extreme weather.
- » Clean energy alternatives, such as district heating, are required to pay such a fee.
- » By not allowing a right-of-way fee for gas infrastructure in Ontario cities, money is left on the table and the cost of gas companies using the infrastructure is shouldered by the public.

NEXT STEPS FOR MUNICIPAL STAFF

- » Identify who in your municipality is in charge of the Model Franchise Agreement, learn more about the history, and build your understanding of the process of updating the Franchise Agreement.
- » Engage with the Property Tax department if property taxes are being collected on the fossil fuel pipelines and infrastructure in your municipality. Explore the potential of collecting property taxes from fossil fuel pipelines if not already being collected with your Tax department.
- » Engage with your Property Tax department to explore the possibility of adding a climate levy if the municipality is collecting property taxes on fossil fuel pipelines and infrastructure.
- » Engage with your Public Works department to explore the costs associated with pipelines regarding road rehabilitation issues and the risk of stranded assets/ infrastructure abandonment.

REFERENCES

[1] In alignment with Ontario's Municipal Energy Plan program which supports comprehensive long-term plans to improve energy efficiency, reduce energy consumption and greenhouse gas emissions, foster green energy solutions and support economic development.

[2] <https://www.ontario.ca/page/made-in-ontario-environment-plan#section-5>

[3] <https://can01.safelinks.protection.outlook.com/?url=https%3A%2F%2Fwww.ontario.ca%2Fflaws%2Fregulation%2F980387&data=02%7C01%7Cjanice.ashworth%40ottawa>.

[4] <https://www150.statcan.gc.ca/t1/tbl1/en/>

[5] Enbridge owns almost 100% of the gas distribution networks in Ontario, with Epcor owning a small portion

[6] <https://www.canada.ca/content/dam/eccc/documents/pdf/climate-change/discussion-document-assessment-framework-inefficient-fossil-fuel-subsidies.pdf>

[7] https://www.edmonton.ca/city_government/documents/TWWF_FranchiseFees_WhitePaper.pdf

[8] <https://sarm.ca/advocacy/resolutions/resolution-full?id=1136>

[9] <http://clkapps.winnipeg.ca/dmis/docext/ViewDoc.asp?DocumentTypeId=1&DocId=204&DocType=C>

