Decision **28244-D01-2023**

Alberta Utilities Commission

The City of Calgary

Decision on Preliminary Question
Application for Review of Decision 26616-D01-2022
2023 Cost-of-Service Review

September 22, 2023

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1 Decision summary

1. In this decision, the Alberta Utilities Commission denies an application by The City of Calgary to review and vary Decision 26616-D01-2022.[1] Calgary's submissions failed to demonstrate that there are changed circumstances material to the decision, which occurred since its issuance, as required under Section 5(1)(c) of Rule 016: *Review of Commission Decisions*.

2 Background

2. Decision 26616-D01-2022 (the Decision) provided the Commission's determinations in respect of the 2023 cost-of-service (COS) applications of ATCO Gas, a division of ATCO Gas and Pipelines Ltd., and Apex Utilities Inc. Calgary was an intervener in the proceeding leading to the Decision.

3. On June 5, 2023, Calgary filed an application to review and vary the Decision pursuant to Section 10 of the *Alberta Utilities Commission Act* and Rule 016 (review application). The review application applied solely to ATCO Gas. Calgary did not seek any relief with respect to Apex. The Commission designated the review application as Proceeding 28244.

4. The Commission issued a filing announcement for the review application and, by letter dated June 28, 2023, established a process schedule for the proceeding. The Commission considers the record for this proceeding to have closed on August 2, 2023.

5. In this decision, the members of the Commission panel who authored the original decision will be referred to as the "hearing panel" and the members of the Commission panel considering the review application will be referred to as the "review panel."

6. The review panel reviewed the entire record in coming to this decision; lack of reference to a matter addressed in the submissions does not mean that the review panel did not consider it.

3 The Commission's review process

7. The Commission's authority to review its own decisions is discretionary and is found in Section 10 of the *Alberta Utilities Commission Act*. Rule 016 sets out the process for considering an application for review. The review process has two stages. In the first stage, a review panel decides if there are grounds to review the original decision (the preliminary question). If the

[1] Decision 26616-D01-2022: ATCO Gas, Apex Utilities Inc., 2023 Cost-of-Service Review, Proceeding 26616, September 1, 2022.

review panel decides to review the decision, it moves to the second stage where it decides whether to confirm, vary, or rescind the original decision (the variance question). In this decision, the review panel has decided the preliminary question.

8. Under Section 5(1) of Rule 016, the Commission may grant an application for a review of a decision where it determines that the review applicant has demonstrated one or more of the grounds set out in that section. Calgary solely relies on Section 5(1)(c) of Rule 016. Under Section 5(1)(c), the review panel may grant an application for a review of a decision, where the applicant has demonstrated that there are changed circumstances material to the decision, which occurred since its issuance.

9. Calgary noted that ATCO Gas exceeded the achieved return on equity (ROE) thresholds for a reopener proceeding to potentially be triggered, as set out in Decision 20414-D01-2016 (Errata).[2] There, the Commission set out a reopener provision allowing for review of the distribution utilities' 2018-2022 performance-based regulation (PBR2) plans if the achieved ROE is 300 basis points above or below the approved ROE for two consecutive years, or 500 basis points above or below the approved ROE in a single year.[3] ATCO Gas filed its 2021 Rule 005: *Annual Reporting Requirements of Financial and Operational Results* filing on May 15, 2022, and its 2022 Rule 005 filing on May 15, 2023. The Commission approved ROE was 8.50 per cent for both 2021 and 2022. ATCO Gas's achieved ROEs of 11.81 per cent and 14.40 per cent for 2021 and 2022, respectively, exceeded the +/-300 basis point reopener threshold for 2021 and 2022, and the +/-500 basis point reopener threshold for 2022.

10. Calgary submitted that the following are changed circumstances that are material to the Decision and occurred since the Decision was issued:

(a) ATCO Gas's 2022 ROE;

(b) ATCO Gas's exceedance of the +/-500 basis point reopener threshold for 2022;

(c) ATCO Gas's exceedance of the +/-300 basis point reopener threshold for 2021 and 2022; and

(d) the events described in (b) and (c) are the second time that ATCO Gas has exceeded those reopener thresholds in the final two years of a performance based regulation (PBR) term, having also done so in the last two years of the first generation PBR term.

[2] Decision 20414-D01-2016 (Errata): 2018-2022 Performance-Based Regulation Plans for Alberta Electric and Gas Distribution Utilities, Proceeding 20414, February 6, 2017.

[3] Decision 20414-D01-2016 (Errata) at paragraphs 279-280. Subject to clarification on the calculation of ROEs, the reopener provision of the 2018-2022 plans was the same as in the first generation PBR plans approved in Decision 2012-237: Rate Regulation Initiative Distribution Performance-Based Regulation, Proceeding 566, Application 1606029, September 12, 2012.

4 Review panel findings

4.1 Timing of the review application

11. Calgary filed the review application outside the 30-day deadline for doing so, as set out in Section 3(3) Rule 016. Calgary did not seek authorization from the Commission to do so. Nevertheless, the review panel has exercised its discretion to consider the application.

4.2 Calgary's characterization of its asserted ground for review

12. Calgary asserted that four separate changed circumstances have occurred. The review panel does not accept this characterization. In the review panel's view the circumstances set out above in subparagraphs 10(b) through (d) are the regulatory consequences of the circumstance set out above in subparagraph 10(a), that is, ATCO Gas's achieved 2022 ROE. ATCO Gas's exceedance of its PBR2 plan reopener thresholds triggers its own regulatory mechanism.

13. Therefore, the only item that the review panel considers can be a changed circumstance for the purposes of Section 5(1)(c) of Rule 016 is ATCO Gas's 2022 achieved ROE. In the remainder of this decision, the review panel will examine whether ATCO Gas's achieved 2022 ROE is a changed circumstance material to the Decision.

4.3 Overview of Decision 26616-D01-2022

14. In Decision 26616-D01-2022 the hearing panel established the 2023 revenue requirement for ATCO Gas's gas distribution utility business. To do so, the hearing panel assessed the reasonableness of ATCO Gas's 2023 forecast costs on a forward-looking basis.

15. ATCO Gas's 2023 rates, derived from its 2023 revenue requirement, are to serve as "going-in rates" for the third generation PBR term (PBR3) that will commence on January 1, 2024. For ATCO Gas, 2023 is an intervening COS "rebasing" year that falls between two PBR terms.

16. The Commission set out how it would process ATCO Gas's and others' 2023 COS applications in Decision 26354-D01-2021.[4] There, the Commission allowed ATCO Gas and others to use a "hybrid approach" to develop their forecasts for the 2023 rebasing year. ATCO Gas employed this approach – which included mechanistic and non-mechanistic components – to forecast its 2023 costs.[5]

17. ATCO Gas filed its 2023 COS rebasing application on December 15, 2021, consistent with the Commission's direction in Decision 26354-D01-2021. The hearing panel started its

[4] Decision 26354-D01-2021: Process to Establish 2023 Rates for Alberta Electric and Gas Distribution Utilities, Proceeding 26354, June 18, 2021.

[5] For its mechanistic approach, ATCO Gas restated its historical actual 2018-2020 costs in 2020 dollars by normalizing for inflation and system size using its I factor inflation and annual customer growth escalators. The restated amounts for the three-years were then averaged. Next, these averaged costs were escalated and restated again, this time in 2023 dollars by normalizing for inflation and system size using ATCO Gas's forecast inflation and annual customer growth rates for the 2021-2023 period. The mechanistic approach was applied to costs that were not expected to fluctuate significantly from the costs incurred over the 2018-2020 period. ATCO Gas applied the non-mechanistic. traditional line-by-line forecasting approach to costs where there was an expected divergence from past years, or the forecast cost was not part of the historical costs structure.

assessment of ATCO Gas's 2023 forecast costs at a time when ATCO Gas's 2018 to 2020 audited financial performance data was available. Data showing ATCO Gas's 2021 actual financial performance became available in May 2022 before the evidentiary record for Proceeding 26616 closed. The hearing panel published the Decision on September 1, 2022, when data for ATCO Gas's 2022 actual financial performance was not yet available.

18. In the Decision, the hearing panel assessed ATCO Gas's forecast 2023 revenue requirement, approving certain forecast costs and denying or directing adjustments to the calculation of others, without the benefit of data showing ATCO Gas's 2022 actual financial performance. The denials of forecast costs included expected costs for ATCO Gas's proposed CIS Replacement Program, and reductions to ATCO Gas's growth and inflation escalators, among other things.

4.4 Assessment of the asserted ground for review

19. There is a two-part analysis for review applications that are grounded on Section 5(1)(c). First, the review applicant must show that there are changed circumstances that have arisen since the original decision was issued. Second, the review applicant must demonstrate that these changed circumstances are material to the original decision.

20. As to the first part, the review panel is satisfied that changed circumstance have occurred since the issuance of the Decision. ATCO Gas's 2022 achieved ROE is a changed circumstance that has occurred since the Decision was issued.

21. The review panel now examines whether this circumstance was material to the Decision and finds that it is not.

22. The hearing panel did not rely whatsoever on data showing ATCO Gas's 2022 actual financial performance in determining whether ATCO Gas's 2023 forecast costs were reasonable. The hearing panel was aware that ATCO Gas's 2022 actual results may differ from what was forecast. It acknowledged that ATCO Gas had earned more than its approved ROE in each of the years of the PBR2 term up to the time the Decision was issued. It recognized that ATCO Gas was entitled to do so under PBR incentives.[6] Indeed, the hearing panel concluded that what ATCO Gas earned or did not earn in the past has no bearing on its statutory right to a reasonable opportunity to earn the approved rate of return in the future.[7] The review panel agrees with this reasoning.

23. While the foregoing is sufficient to determine that ATCO Gas's achieved 2022 ROE is not material to the Decision, the review panel has nevertheless considered Calgary's argument that the hearing panel's understanding of the incentives embedded in PBR is flawed. In the Decision, the hearing panel noted that there is a weakening of the incentive to pursue efficiencies in the final year of a PBR plan because there is less time remaining for the distribution utility to benefit from any efficiency gain and, concomitantly, that distribution utilities are incentivized to increase their costs in the final year of a PBR plan in order to increase going-in rates for the next

6 Decision, paragraph 47.
7 Decision, paragraph 47.

PBR term. Calgary contended that ATCO Gas's actual results call into question the validity of the hearing panel's understanding of these incentives.

24. The review panel does not find Calgary's argument persuasive. ATCO Gas's actual results do not change the underlying premise that the incentive to pursue efficiencies embedded in a PBR plan weakens in the final year of a plan because the distribution utility will enjoy the benefit of any efficiencies achieved for only one year. In contrast, the benefit of any efficiencies found by a distribution utility at the start of a PBR plan will be enjoyed by the distribution utility for the entire remainder of the PBR term. This incentive structure is embedded in the plan design and is unaffected by ATCO Gas's actual results.

25. The review panel also notes that other incentives exist in ATCO Gas's PBR2 plan, which may incentivize ATCO Gas to continue to search for efficiencies in the final year of a PBR plan. For example, the Commission approved an efficiency carryover mechanism (ECM) in ATCO Gas's PBR2 plan to address the weakening of the incentive to pursue efficiencies towards the end of a PBR term. The ECM allows the distribution utilities to carry a portion of earnings in excess of the approved ROE from one PBR term to the next,[8] thereby incentivizing the distribution utilities to continue to pursue efficiencies while diminishing the incentive to increase costs in the final year of a PBR plan.

26. Relatedly, in the Decision, the hearing panel was mindful of certain potentially problematic incentives associated with the rebasing process, including concerns that setting going-in rates in a COS proceeding based on forecast costs may create incentives to over-forecast, with the result that customers do not share in the benefits of productivity gains achieved by the distribution utilities in the prior PBR period. The hearing panel took steps to address those concerns by specifically requesting ATCO Gas to quantify and clearly demonstrate how efficiencies found, and cost reductions achieved, during the PBR2 term were reflected in its forecast revenue requirement and would be passed on to customers.[9]

27. Various incentives related to the PBR2 plans and the rebasing process were considered by the hearing panel as it was required to evaluate the reasonableness of ATCO Gas's forecast revenue requirements to set rates on a *prospective* basis. The hearing panel emphasized the importance of prospective rate-setting noting that it: (i) reduces regulatory lag, (ii) enables the utilities to manage their actual costs to their respective forecasts and to respond to the incentives built into their approved PBR plans, (iii) provides the utilities and their consumers with certainty by avoiding retrospective adjustments to rate base, and (iv) is consistent with the Commission's past approach to setting rates under a COS framework.[10] The hearing panel made the decision to set ATCO Gas's going-in rates for the next PBR term (PBR3) on a prospective basis with full knowledge that ATCO Gas's 2022 actual costs would not be available prior to the issuance of the Decision.[11]

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8 Specifically, the ECM ROE add-on is calculated as 50 per cent of the difference between the average allowed and average actual ROEs over the course of the PBR term, with an upper limit of 0.5 percentage points: Decision 2012-237, paragraph 766 as clarified in Decision 20414-D01-2016 (Errata), paragraph 79.

9 Decision, paragraph 43.

10 Decision, paragraphs 57-58.

11 See e.g. Decision at paragraphs 145, 147. ATCO Gas's 2021 actual costs were not available at the time of application filing, but non-audited and audited 2021 actual costs were filed prior to the issuance of the Decision

28. Finally, it is worth noting that ATCO Gas's customers will share in the capital cost savings realized by ATCO Gas in PBR2 even though ATCO Gas's 2022 actual costs were not considered by the hearing panel. In the Decision, the hearing panel confirmed that ATCO Gas's 2023 opening rate base would receive placeholder treatment because the 2021 and 2022 actual capital inputs and 2022 actual closing rate base were not available at the time ATCO Gas filed its application. ATCO Gas's 2023 opening rate base will be finalized based on final actual amounts, which are subject to Commission review for prudence.[12] Accordingly, ATCO Gas's capital cost savings realized during the PBR2 term will reduce ATCO Gas's future revenue requirements.

29. ATCO Gas's actual 2023 opening rate base will also affect ATCO Gas's going-in rates for PBR3. ATCO Gas's going-in rate for PBR3 will be determined by averaging its 2023 opening rate base and 2023 forecast closing rate base that was approved in the Decision (which included the denial of certain forecast capital additions noted in paragraph 18, above). Any changes or adjustments to ATCO Gas's 2023 revenue requirements as a result of the finalization of the 2023 opening rate base will subsequently be trued up as part of an annual PBR rate adjustment filing.

30. Based on the foregoing, Calgary has not demonstrated to the review panel that ATCO Gas's 2022 achieved ROE is a changed circumstance that is material to the Decision.

31. The review panel observes that the Commission is examining ATCO Gas's 2021 and 2022 actual results in Proceeding 28300. The Commission initiated that proceeding to consider whether to reopen and review ATCO Gas's PBR2 plan based on essentially the same circumstances as those precipitating Calgary's review and variance application being determined here, that is, on account of ATCO Gas having exceeded the achieved ROE thresholds for a reopener proceeding in the last two years of its PBR2 term.

4.5 Procedural concerns raised by ATCO Gas

32. On August 2, 2023, ATCO Gas wrote to the review panel to object to Calgary's reply submission. Given the assessment in Section 4.3, the review panel does not need to rule on ATCO Gas's motion. Nevertheless, the review panel notes that Calgary's reply submission was non-compliant with Rule 016 on account of its excessive length.

(in April and May of 2022, respectively). The Commission did not require the utilities to do a comprehensive update of their applications; however, the utilities did provide detailed tables setting out their 2021 actual capital costs accompanied by variance explanations in relation to filed 2021 forecasts.

12 Decision at paras 238-241. The hearing panel reviewed ATCO Gas's non-audited 2021 actual costs and accepted them as prudently incurred unless noted otherwise in the Decision. This finding was subject to the Commission's review of ATCO Gas's explanations for any variances between the non-audited 2021 actual expenditures filed in Proceeding 26616 in April 2022 and audited costs reported in 2021 Rule 005 filings. The hearing panel also noted that the Commission may examine any variances between the actual opening 2023 rate base and the 2022 placeholder amount in a future proceeding, which could result in disallowances and potential changes to going-in rates if the Commission is not persuaded that the 2022 actual capital additions were prudent.

5 Decision

33. In answering the preliminary question, the review panel finds that The City of Calgary has not met the requirements for a review of the Decision and the application for review is dismissed.

Dated on September 22, 2023.

Alberta Utilities Commission

(original signed by)

Douglas A. Larder, KC
Vice-Chair

(original signed by)

Bohdan (Don) Romaniuk
Acting Commission Member