Fasken Martineau DuMoulin LLP *
Barristers and Solicitors
Patent and Trade-mark Agents

2900 – 550 Burrard Street
Vancouver, British Columbia, Canada V6C 0A3

604 631 3131 Telephone
604 631 3232 Facsimile
1 866 635 3131 Toll free

www.fasken.com

Matthew Ghikas
Direct 604 631 3191
Facsimile 604 632 3191
mghikas@fasken.com

April 25, 2014
File No.: 240148.00723/14797

BY E-MAIL

British Columbia Utilities Commission
6th floor, 900 Howe Street
Vancouver, BC V6Z 2N3

Attention: Erica Hamilton
Commission Secretary

Dear Sirs/Mesdames:

Re: FortisBC Energy Inc. and FortisBC Inc. Applications for Approval of a Multi-Year Performance Based Ratemaking Plan for 2014 through 2018

The Companies Joint PBR Submission

We enclose for filing in the above proceedings the electronic versions of

1. the Joint Final Submission of FortisBC Energy Inc. ("FEI") and FortisBC Inc. ("FBC") on PBR Plan Design dated April 25, 2014 ("PBR Submission").

2. a legal authority cited in the PBR Submission.

Sixteen hard copies will follow by courier.

This is one of three submissions being filed contemporaneously by the Companies. Each of FBC and FEI will also be filing separate submissions on non-PBR issues.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP

[Original signed by Matthew Ghikas]

Matthew Ghikas

MTG/fxm
Enc

BRITISH COLUMBIA UTILITIES COMMISSION

IN THE MATTER OF THE UTILITIES COMMISSION ACT,

R.S.B.C. 1996, CHAPTER 473

and

RE: FORTISBC ENERGY INC. and FORTISBC INC.

APPLICATIONS FOR APPROVAL OF A MULTI-YEAR PERFORMANCE BASED RATEMAKING PLAN FOR 2014 THROUGH 2018

JOINT FINAL SUBMISSION OF FORTISBC ENERGY INC. and FORTISBC INC. ON PBR PLAN DESIGN

April 25, 2014

TABLE OF CONTENTS

PART ONE: INTRODUCTION AND OVERVIEW

1. This joint submission (the "PBR Submission") of FortisBC Energy Inc. ("FEI") and FortisBC Inc. ("FBC", and together with FEI, the "Companies", "FortisBC" or "FortisBC Utilities") addresses the design of the proposed multi-year performance based ratemaking ("PBR") plan (the "PBR Plan"). It should be read in conjunction with the submissions filed contemporaneously by each of FEI and FBC that address the issues not directly related to the PBR Plan ("Non-PBR Submissions").

A. INTRODUCTION

2. There is a sound economic basis for PBR. Past experience underscores that PBR presents an opportunity for customers and the FortisBC Utilities to benefit from (a) the Companies being able to take a longer-term view in finding incremental savings, while maintaining their high level of service quality, and (b) cost savings associated with improved regulatory efficiency.[1]

3. FortisBC developed its proposed PBR Plan, which is described in Section B6 of the FEI and FBC Applications,[2] in conjunction with a highly knowledgeable PBR expert in Dr. Overcast.[3] The proposed PBR Plan builds on the Companies' successful past PBR plans, with some improvements. There are no obvious benefits, and disadvantages, with importing a new approach, wholesale, from other jurisdictions. Plans in other jurisdictions are themselves customized to fit the circumstances of the utilities subject to those plans. Building on the Companies' past success maximizes the prospects that this PBR will also be a success.

4. The PBR Plan meets widely accepted and applied PBR principles. It provides a fair and balanced allocation of risks and benefits, as reflected in (among other things) a formula

---

[1] The benefits of PBR generally are addressed in FEI Exhibit B-1, FEI Application, p.29.

[2] A useful summary of the Plan appears in the table on p.44 of the FEI Application (FEI Exhibit B-1).

[3] T2:222, ll.19-24 (Overcast).

that includes a productivity improvement factor to provide immediate benefits to customers, and a symmetrical approach to earnings sharing, the Efficiency Carry-over Mechanism and Off-ramps. It ensures that FortisBC will continue to provide high quality, reliable and cost-effective service, and will provide an opportunity for the Companies to earn a fair return. The overall PBR Plan is just and reasonable and should be approved under sections 59-61 of the *Utilities Commission Act* ("UCA").

B. OVERVIEW OF PBR SUBMISSION

5. This PBR Submission is organized as follows:

- Part Two addresses how the Commission should approach its review of the PBR Plan.
- Part Three addresses individual components of the PBR Plan, other than the I-X formula and Service Quality Indicators ("SQIs").
- Part Four addresses the I-X formula. It explains why the proposed method of forecasting inflation during the PBR period is reasonable. It also explains why the proposed X-Factor of 0.5% poses a significant productivity challenge to the Companies, and why Dr. Lowry's approach yields an excessive X-Factor.
- Part Five speaks to why customers can expect FortisBC to maintain the current high level of service quality.
- Part Six is a conclusion.

PART TWO: APPROACH TO ASSESSING THE PBR PLAN

6. Part Two of this PBR Submission addresses how, in FortisBC's submission, the Commission should approach its assessment of the PBR Plan. We make a number of points:

- First, there is a sound economic basis for PBR, and the results of the Companies' past PBR plans confirm that a well-designed and comprehensive PBR will deliver benefits to both customers and the Companies.

- Second, similar principles are applied across jurisdictions in designing PBR plans, and FortisBC has appropriately applied those principles to its own circumstances.

- Third, PBR is subject to the same legal framework and ratemaking principles as traditional cost of service ("COS") ratemaking. Key recommendations of intervener experts run afoul of the UCA.

- Fourth, building on the long and successful experience with PBR in BC maximizes the potential for this PBR to benefit all stakeholders.

A. THE LOGIC OF PBR

7. The Companies presented expert evidence on the economic and regulatory principles underpinning PBR generally, as well as evidence based on FortisBC's past experience. The evidence demonstrates that:

- there is a sound economic rationale for adopting PBR at this time, which includes improved regulatory efficiency and a larger pool of potential efficiencies; and

- the primary arguments advanced in opposition to PBR are without merit.

(a) Rationale for Adopting PBR

8. Dr. Overcast provided expert evidence on the logic of PBR. He is well qualified to speak to both the theory of PBR and its practical application to the Companies, based on his experience with PBR and his understanding of utility economics.[4] The two most commonly cited benefits of PBR, relative to traditional cost of service regulation, are improved regulatory efficiency and expanding the potential pool of incremental savings from efficiencies. The proposed PBR Plan will deliver both benefits, given its design.

Improved Regulatory Efficiency

9. Improved Regulatory efficiency provides direct cost savings and indirect benefits.

10. The direct cost savings associated with the adoption of the PBR Plan will be significant. The Companies estimate that the avoided incremental costs over the PBR term that are captured in deferral accounts, compared to cost of service regulation, could be up to $2 million annually, not accounting for internal costs.[5] The cost has a disproportionately large impact on FBC and its customers, since it is a smaller utility. Mr. Swanson indicated: "if we were unsuccessful in obtaining a PBR and it had to go through regular revenue requirements process, each one of those processes would add approximately 1 percent to the rate increase."[6] The extent of the direct savings that will result from avoiding the costs of full revenue requirement proceedings will depend to some degree on how efficiently the Annual Review and Mid-term Review processes are conducted. However, the proposed PBR Plan positions stakeholders to achieve significant savings through streamlined reviews because the regulatory

---

[4] Dr. Overcast's CV is found in FEI Exhibit B-1-1, Appendix D3. His qualifications were discussed starting at T2: 219, l.9. Dr. Overcast has a PhD in economics. He has been involved in developing many PBR plans for utilities across North America. He also held senior positions in electric and gas utilities for many years, where he gained first-hand experience of the type of decisions that a utility must make to find efficiencies under PBR.

[5] Exhibit B2-8, BCUC-FEI/FBC IR 3.5.5; FEI Exhibit B-23, CEC-FEI IR 2.75.1.1. T3:431, l.10-432, l.19 (Swanson). There is no cost included in the forecasts in this proceeding for holding RRA processes during the next five years. Internal costs are embedded in O&M: T3:435, ll.15-26 (Roy).

[6] T3:433, ll.2-4 (Swanson).

process around revenue requirements proceedings is typically focussed on costs that will be replaced with a pre-determined formula in PBR.[7]

11. The indirect benefit of a more streamlined regulatory process is frequently overlooked, but is equally important. Managing the regulatory process requires a huge investment of corporate resources and personnel time. FortisBC accepts the necessity of this investment, given that it provides a regulated service. However, PBR has the potential to free-up individuals within the Companies to focus more on managing the utility business more efficiently. Dr. Overcast and Ms. Roy explained:

> DR. OVERCAST: … And there's one added benefit that we haven't really talked about. If you look around this room at all the people that are here, this represents a fraction of the number of people in the company who are involved in a cost of service proceeding.
>
> I mean, you've got all these talented people who understand the business spending all their time developing a cost of service, coming up here and defending it, and under PBR those same people, the people who know the business best, they can devote their time to figuring out ways to make the company more efficient instead of presenting a big application and answering thousands of interrogatories. It's -- there is that advantage of PBR. And that's a huge advantage as well. You get your best people, with your best minds, working on finding a better way to operate.
>
> MS. ROY: A: And I think Dr. Overcast has actually stepped on exactly the comment I was going to make, is that first of all if you look at our application, you can tell that we have actually invested in efficiencies even in cost of service period. So, yeah, we are always looking to operate efficiency. That's true. But what PBR does is, it allows us to shift our focus -- or the management focus. Because suddenly everybody is not busy trying to get ready for applications, or go to hearings, or, you know, justify costs before the regulator. And it broadens the scope of what we're allowed to look at, or what we can look at, not just by providing us with a longer period to look at those over, but just freeing up every department, and every person in the company, to actually be looking at running the business. You know, and that's on top of really just the savings in regulatory costs that Dr. Overcast referred to.

[7] T3:442, l.3-443, l.26 (Swanson).

> You know, as we said before, we have an IR where we talk about the annual reviews cost anywhere from $5,000 to $35,000 for FEI, and it was $35,000 to $70,000 for FBC last time around. And these processes are millions of dollars, and a lot of time. So that's on top of the efficiencies that just come from, you know, the minds of the people working in the business itself.[8]

Increasing the Pool of Potential Efficiency Savings

12. The other rationale for PBR is achieving savings from incremental efficiencies throughout the organization. Incentives exist under COS ratemaking for the utility to seek out savings and act efficiently. FortisBC's "history will show that both companies have been diligent in trying to achieve savings where savings are available."[9] Nevertheless, PBR inherently opens up new opportunities for the utility to find efficiencies.

13. Dr. Overcast explained that, although the utility is motivated to "operate as efficiently as they can possibly operate" under COS ratemaking and PBR, the utility's need to obtain a payback on efficiency investments is a practical constraint on its ability to invest in incremental efficiencies under any regulatory model.[10] If the payback period for an investment to improve efficiency is longer than the period until rebasing, then the shareholder will not obtain a full return of and on that investment.[11] In the absence of some other compelling business reason, investing in efficiencies that do not have a prospect of achieving an appropriate payback before rebasing would not represent sound management. As Dr. Overcast put it: "it's not the way companies operate."[12]

14. The pool of potential efficiencies that is available to be pursued is inherently going to be larger under PBR than under COS regulation. The longer term of the PBR Plan relative to a typical test period increases the time available before rebasing for the utility to obtain a payback on investments in incremental efficiencies. Dr. Overcast, when asked to

---

8 T3:403, l.16-405, l.7 (Swanson).

9 T2:303, ll.1-5 (Swanson).

10 T3:402, ll. 1-11 (Overcast).

11 T4:733, l.16-734, l.9 (Overcast).

12 T2:343, ll.6-17 (Overcast). See also: T3:402, l.1-403, l.15 (Overcast).

explain his view that there will be efficiencies achieved under a PBR mechanism that will not be achieved under a traditional COS regulation, explained:[13]

> It's really more than a view. It's the way the system operates. If you only have one year, you're limited to efficiency investments that have a payback less than one year. If you have a five-year PBR plan, your set of potential incentives expands from those with a one-year payback to those with a five-year payback. And obviously the second set is larger than the first set.

Dr. Overcast provided an example at the hearing of how a utility investing in efficiency improvements can lose money upon rebasing despite there being a regulated rate of return on invested capital.[14]

15. It is possible under COS regulation to accommodate longer-term costs and savings associated with efficiency investments, but they must be identified in advance and be reflected in a revenue requirements application. Dr. Overcast stated that "the operation of a utility is much more fluid than that, so you may be actually eliminating things that might have even been better, just because you can forecast one but you can't forecast the other."[15]

16. The results of the past PBR plans underscore that PBR creates new opportunities to find efficiencies, and that the Companies will exercise diligence in achieving available efficiencies:

- ***FEI:*** FEI achieved $45 million in O&M savings during the 2004-2009 FEI PBR (the "2004 FEI PBR") due to the productivity factor (i.e. X-Factor) alone, which went 100% to customers. FEI also achieved $137 million of savings above the X-Factor that were shared with customers during the PBR term. The savings achieved during PBR were then rebased into lower rates coming out of the PBR term, which sustained the benefits.[16] In FEI's 2012-2013 RRA the Commission

[13] T2:342, l.21-343, l.2 (Overcast).

[14] T2:344, l.8 - 346, l.6 (Overcast).

[15] T2:347, ll.14-24 (Overcast). See also: T3:399, ll.3-20 (Swanson).

[16] T2:234, ll.2-12 (Roy).

examined the results of the 2004 FEI PBR Plan and concluded that significant benefits were achieved for both customers and the utility:

> In British Columbia, PBR, combined with the Negotiated Settlement Process has played a role within the rate setting process of FEI. Starting in 2004 and lasting through 2009 FEI operated in a PBR environment. During this period FEI was very successful as targets were met and the Companies note that shared earnings benefits flowing to customers and shareholders totalled $67.5 million each over the six years.
>
> The Commission Panel is satisfied that there were positive results experienced by both ratepayers and the shareholder over the PBR period. In addition, the Panel finds there is sufficient evidence to suggest that introducing a PBR environment has the potential to act as an incentive to create productivity improvements.[17]
>
> ….
>
> As noted in section 4.2, the Commission recognizes that during the PBR period FEI was able to find significant cost savings to the benefit of customers and the shareholder. During this six-year period $67.5 million in benefits flowed to customers, while an equal amount flowed to the shareholder.[18]

- ***FBC***: Material efficiencies of 10.4 percent were embedded in FBC's O&M expense by way of negotiated "productivity improvement factors" during its last PBR period from 2007 to 2011 (the "2007 FBC PBR").[19] This cumulative percentage increased to 27.5% for the last 15 years.[20]

17. Mr. Swanson stated during the Companies' opening presentation that the Companies could be expected to respond to the incentives inherent in the proposed PBR Plan in

---

[17] *In the Matter of the FortisBC Energy Utilities [comprised of FortisBC Energy Inc., FortisBC Energy Inc. Fort Nelson Service Area, FortisBC Energy (Vancouver Island) Inc. and FortisBC Energy (Whistler) Inc.] 2012-2013 Revenue Requirements and Rates* Decision, Commission Order No. G-44-12, April 12, 2012 (the "FEU 2012-2013 RRA Decision"), p.22.

[18] FEU 2012-2013 RRA Decision, p. 34.

[19] FBC Exhibit B-1, FBC Application, p.54; T3:421, ll.4-26 (Swanson).

[20] T2:324, ll.19-25 (Swanson).

a similar manner as before.[21] That is, the Companies expect to delve into all aspects of the business looking for a series of smaller incremental savings that can add up to significant benefits. [22]

(b) Addressing Arguments Against PBR

18. Some parties appear to be skeptical of PBR generally. Their arguments against PBR centred on the two themes, addressed below, neither of which has merit.

The Idea that Utilities Should Seek Incremental Efficiencies Anyway

19. It was evident from some of the information requests that there is a view among some interveners that PBR is unnecessary because utilities would or should be seeking efficiencies anyway. This suggestion, with respect, misses the mark. As described above, utilities are incented to act efficiently under either COS or PBR. However, in order for the utility to have an opportunity to achieve its allowed return under COS regulation its investments in efficiencies must either be forecasted or have a payback period shorter than the test period.[23] The Supreme Court of Canada, in the *ATCO* decision,[24] dispelled the misperception that utilities should be operated without regard to considerations such as the ability to earn a fair return on and of invested capital. The Court stated for instance:

> 4 As in any business venture, public utilities make business decisions, their ultimate goal being to maximize the residual benefits to shareholders. However, the regulator limits the utility's managerial discretion over key decisions, including prices, service offerings and the prudency of plant and equipment investment decisions. And more relevant to this case, the utility, outside the ordinary course of business, is limited in its right to sell assets it owns: it must obtain authorization from its regulator before selling an asset previously used to produce regulated services.

---

[21] T2:245, l.19-246, l.8 (Swanson).

[22] T3:395, l.20-396, l.4 (Swanson).

[23] T3:400, l.13-403, l.15 (Swanson, Overcast); T3:534, ll.2-11 (Swanson).

[24] *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, 2006 SCC 4 ("*ATCO*"), at paras. 4 and 70. (online at: http://www.canlii.org/en/ca/scc/doc/2006/2006scc4/2006scc4.html).

…

> 70 Furthermore, one has to recognize that utilities are not Crown entities, fraternal societies or cooperatives, or mutual companies, although they have a "public interest" aspect which is to supply the public with a necessary service (in the present case, the provision of natural gas). The capital invested is not provided by the public purse or by the customers; it is injected into the business by private parties who expect as large a return on the capital invested in the enterprise as they would receive if they were investing in other securities possessing equal features of attractiveness, stability and certainty, [Emphasis added; citations omitted.]

20. The idea that the Companies should be investing in efficiencies without a reasonable expectation of payback prior to rebasing is at odds with the Court's reasoning. There is ample evidence on the record for the Commission to conclude that a well-designed PBR is beneficial for both customers and the Companies by increasing the pool of available cost-effective efficiency investments.

The Theme that PBR Results in Customers Paying Twice for Costs

21. The idea that PBR can result in the utility deferring costs, retaining half of the savings, and then recovering the costs in full after the end of the PBR term is a theme that has been raised on a number of occasions by stakeholders since the last FEI and FBC PBRs. The Commission should treat this risk as being no more than theoretical under the proposed PBR Plan.

22. First, there is every reason to expect that the savings will be achieved through sustainable efficiencies, not cost deferrals. The evidence is:

- Appendix D4 demonstrated that no material cost deferrals occurred in the last FEI PBR. The significant benefits achieved for customers and the utility were the product of sustainable savings that continue to be reflected in the base year costs.

- FortisBC and its witnesses emphasized that the Companies intended to focus on sustainable savings under this PBR as well. Ms. Roy stated, for example, that the focus will be on "finding more efficient ways to put the assets into the ground", not on "cutting scope".[25] Mr. Swanson echoed that FortisBC "has no intention" to defer costs.[26] Mr. Pataki, who is a Director responsible for gas operations, put it even more forcefully. His strong reaction to this idea that FortisBC would defer necessary maintenance and sustainment capital spending, contrary to his own professional obligations and CSA guidelines, should leave no doubt that FortisBC's management intends to act appropriately.[27]

- The Companies have put forward long-term capital sustainment plans and have made a significant investment in moving that forward. The forecasted capital reflects that FortisBC intends to continue pursuing its capital plan.

- The Companies "have invested in assets that have a very long lifespan. And in order to earn our return of and return on the capital associated with those assets with a long life span, it requires a long-term relationship with our regulator and with our stakeholders."[28]

- The same risk would exist under COS ratemaking because rates are set on a forecast basis and the utility would retain the entirety of any underspending. In other words, the time period would be shorter under COS, but the amount of benefit that would accrue to the shareholder for each dollar deferred would be twice the benefit as under a 50%/50% ESM. There is no evidence that this has been occurring.

---

[25] T3:475, ll.3-7 (Roy).

[26] T3:475, l.19-476, l.7 (Swanson); T3: 479, ll11-14 (Swanson).

[27] T5:1033, l. 26 – 1036, l.6 (Pataki).

[28] T3:475, ll19-25 (Swanson).

23. Second, the argument disregards the financial implications of a deferred expenditure. Customers would actually benefit in many circumstances if, contrary to all indications, the Companies were to defer expenditures until after PBR in a way that did not otherwise undermine longer-term asset health.[29]

24. Third, there are appropriate regulatory mechanisms in place to address the theoretical risk that FortisBC will defer costs to the detriment of customers or long-term asset health. The Companies have incorporated limited rebasing of capital in the proposal to set a cap on the amount of savings that can be generated from capital cost reductions.[30] Post-PBR the Commission will review Companies' cost structure and FortisBC will have to justify any increases in order for those costs to be reflected in approved COS-based rates.[31]

25. It is a fundamental principle of regulatory law that the utility must be presumed to be acting in good faith. The following passage from the Supreme Court of Canada's decision in *ATCO* is dispositive in this context: "Moreover, in the absence of any factual basis to support it, I am also concerned with the presumption of bad faith on the part of ATCO that appears to underlie the Board's determination to protect the public from some possible future menace."[32] This argument of interveners is based on nothing more than unfounded suspicion of "some possible future menace", and must be rejected.

B. PRINCIPLES REFLECTED IN PBR PLAN

26. In developing the PBR Plan, the FortisBC Utilities were guided by five principles.[33] Dr. Overcast confirmed that the substance of these principles is consistent across jurisdictions, although they are often articulated somewhat differently.[34] FortisBC's guiding principles, and examples of how the Companies have reflected these principles in the overall PBR Plan design,

---

[29] FEI Exhibit B-1-1, FEI Application, Appendix D4.

[30] T3:563, ll.13-20 (Roy).

[31] FEI Exhibit B-8, CEC-FEI IR 1.44.1.

[32] ATCO, *supra*, para. 84.

[33] FEI Exhibit B-1, FEI Application, p.43.

[34] FEI Exhibit B-1, FEI Application, p.43.

are addressed below. FortisBC's adherence to broadly accepted principles is a factor that supports the adoption of the overall PBR Plan.

- ***Principle 1: The PBR plan should, to the greatest extent possible, align the interests of customers and the utility; customers and the utility should share in the benefits of the PBR plan.***

  Customers can expect to benefit under the proposed PBR Plan in three ways.

  First, there are direct and indirect benefits to customers associated with the avoided incremental regulatory process.

  Second, the use of a formula that includes a productivity improvement factor (X-Factor) provides immediate benefits to customers, irrespective of the Companies' performance.

  Third, the symmetrical Earnings Sharing Mechanism ("ESM") presents a prospect for customers and shareholders to share earnings generated from additional savings.[35] Under traditional COS ratemaking, the Commission sets rates based on a forecast. For those costs not subject to deferral treatment, the utility bears the risk of positive cost variances and obtains 100% of the benefit of any savings achieved relative to the forecast. With the ESM, customers benefit from half of any additional earnings achieved above the formula driven amount. Both customers and the Companies are better off if the utility succeeds in finding incremental savings. The off-ramps are symmetrical and temper the potential for unreasonable profits or losses.

- ***Principle 2: The PBR plan must provide the utility with a reasonable opportunity to recover its prudently incurred costs including a fair rate of return.***

[35] T3:446, ll.12-18 (Swanson).

This principle is, in fact, a well-established legal requirement. The next section of this PBR Submission addresses the applicable legal test and how the proposed PBR Plan meets the legal test.

- ***Principle 3: The PBR plan should recognize the unique circumstances of the Company that are relevant to the PBR design.***

  FortisBC retained Dr. Overcast to perform a survey of PBR plans in other Canadian jurisdictions.[36] Dr. Overcast is also familiar with PBR plans in the United States and Australia. His research demonstrates that PBRs generally incorporate an I-X formula[37], but within that general framework there are different ways of structuring a PBR plan. The common thread is that each jurisdiction is adapting PBR to fit its own unique requirements. Dr. Overcast's findings support FortisBC's decision to base the proposed PBR Plan is based on earlier plans in BC that met the requirements of the Commission and stakeholders, with some enhancements.

  Although the PBR Plan is being applied in a similar fashion both FEI and FBC, it accommodates differences between the two utilities. Each utility's unique "lumpy" capital expenditures will be addressed outside of the formula-based capital spending allowances. FEI's and FBC's approved CPCN criteria define the limits of excluded capital, and the CPCNs act as a form of "capital tracker" mechanism. FEI and FBC also have unique flow-through items to reflect the different nature of their uncontrollable costs. There are differences in how growth is reflected in capital, given the cost drivers applicable to each utility. It otherwise makes sense to employ a common PBR Plan, given the common management structure in place.

[36] FEI Exhibit B-1-1, FEI Application, Appendix D1; FBC Exhibit B-1-1, FBC Application, Appendix D1.

[37] FEI Exhibit B-1, FEI Application, p.32.

- ***Principle 4: The PBR plan should maintain the utility's focus on maintaining safe, reliable service and customer service quality while creating the efficiency incentives to continue with its productivity improvement culture.***

  A PBR, by its nature, increases the available pool of cost-effective efficiency investments. The proposed PBR Plan incorporates an I-X formula, where the X-Factor is a productivity improvement factor that drives the efficiency investments. As described in Part 4 of this PBR Submission, the X-Factor of 0.5% is based on (a) a calculation of industry-wide productivity levels as a starting point, (b) an upward adjustment to account for the exclusion of CPCN capital and flow-throughs from the formula, and (c) a further upward adjustment in the form of a "stretch factor". The practical result of the proposed X-Factor is that the trajectory of the formula-driven revenue during the PBR period will be below the rate of inflation. Customers benefit immediately through formula-driven rates that incorporate a productivity factor, and the Companies will have to find the necessary cost savings to meet or beat this rate trajectory without sacrificing safety, reliability and customer service.[38] The Companies will be reporting on SQIs, and will be answerable for the results, in the manner discussed in Part 5 below.

- ***Principle 5: The PBR plan should be easy to understand, implement and administer and should reduce the regulatory burden over time.***

  Enhanced regulatory efficiency is a very significant potential benefit of PBR, for the reasons described earlier. The potential to realize regulatory efficiency benefits improves when stakeholders are familiar with how the PBR is intended to function. This is a benefit of basing the PBR Plan on past approved PBR plans, and making incremental improvements. While the proposed PBR Plan shares common elements with plans in other jurisdictions, FortisBC has preferred

[38] There is a general discussion on how customers benefit from PBR on p.29 of the FEI Application (FEI Exhibit B-1).

continuity with the past experience in circumstances where there are no obvious benefits, and possibly disadvantages, associated with adopting a new approach employed in the plans in other jurisdictions.[39]

The regulatory oversight mechanisms incorporated in the proposed PBR Plan - the Annual Review and Mid-term Review - were also employed in prior plans. The proposal recognizes that an extensive reporting and compliance framework that delves into how savings are being achieved would undermine the regulatory efficiency benefit associated with PBR. The proposed format has already been proven to be effective in providing a level of oversight commensurate with PBR objectives.

27. In summary, the proposed PBR Plan advances these principles, which supports the acceptance of the PBR Plan as a whole.

C. SAME LEGAL FRAMEWORK APPLIES TO PBR AS COST OF SERVICE REGULATION

28. FortisBC discusses below how the rates yielded by the PBR Plan, i.e. considering the elements of the PBR Plan holistically, must meet the same legal requirements as rates set under COS regulation. Significant aspects of the intervener evidence filed in this proceeding run afoul of the legal requirements for setting just and reasonable rates, as adoption of their proposals would deny the Companies' opportunity to earn a fair return.

(a) Just and Reasonable Rates in the Context of PBR

29. The Commission is tasked with setting just and reasonable rates under sections 59 to 61 of the UCA, irrespective of whether it is setting rates based on cost of service or according to a PBR plan. A successful PBR Plan integrates a careful balance of provisions that collectively allocate benefits and risks fairly between customers and the Companies.

[39] FEI Exhibit B-1, FEI Application, p.43.

Requirements of the UCA and Regulatory Compact

30. As reflected in section 59(5), just and reasonable rates must represent:

- a "fair and reasonable charge for service of the nature and quality provided by the utility"; and
- "a fair and reasonable compensation for the service provided by the utility", including the Companies' well-established right to an opportunity to earn a fair return.

31. As the rate levels under PBR are the product of all elements of the PBR Plan working in tandem to yield an annual revenue requirement, the PBR Plan should be evaluated on a holistic basis. Dr. Overcast expressed the concept of just and reasonable rates as they relate to PBR in the following economic terms:

> The need for just and reasonable rates under a PBR plan means that each element of the plan must be carefully reviewed so the expectation is that during the regulatory control period a utility operating at the industry average efficiency could expect to earn its allowed rate of return. If the utility operates below the average efficiency it could not reasonably expect to earn the allowed rate of return, but the resulting lower returns should not be so low as to be confiscatory in nature. For performance above the average efficiency, the utility should be able to earn above the allowed rate of return and beyond a reasonable level the customers should benefit directly in the success of the utility at an improved efficiency level. Customers actually benefit even in the absence of an earnings sharing mechanism by a reset of the cost basis of rates at the start of a new regulatory control period as the efficiency gains become entrenched in the utility's revenue requirements on a going forward basis.[40]

FortisBC submits that this is a reasonable way of applying the statutory standard in the context of PBR.

[40] Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.7.

32. In practice, three conditions must be present for the PBR Plan to meet the legislative requirements and ensure that the revenue generated under PBR will permit the FortisBC Utilities to reasonably provide the expected level of service and achieve a fair return:

- First, there must be an appropriate base, or starting level of rates, on which to apply the formula during the PBR Period;
- Second, the PBR plan itself must be crafted recognizing the extent to which costs are within the utilities' control (so as to be capable of being influenced by efficiency incentives); and
- Third, the I-X Formula applicable to controllable costs must realistically portray (a) the impact of inflation (I-Factor) on the cost of various inputs to production, and (b) the various other productivity factors that impact the way costs change over time (X-Factor).[41] The I-X result must be reasonably achievable.

33. These principles and considerations are reflected in the proposed PBR Plan. The base year costs were vetted in the most recent revenue requirements proceedings (and in many respects were re-vetted in this proceeding as well, as discussed in the Non-PBR Submissions of FEI and FBC). The proposed PBR Plan, like the prior FEI and FBC PBR plans, targets efficiency incentives at O&M and capital expenditures, over which the FortisBC Utilities have the greatest influence. The I-X-mechanism represents a fair productivity challenge that delivers immediate benefits to customers. For those items over which FEI has limited or no control, the PBR Plan maintains the same regulatory treatment as was used in the 2004 Plan; they are excluded from the formula using flow-through mechanisms and annual reforecasting, as well as by way of CPCN treatment for large capital projects.[42]

[41] Exhibit B-45, Overcast Rebuttal Evidence, p.5.

[42] FEI Exhibit B-1, FEI Application, p.27.

PBR Plan Must Be Assessed Holistically

34. Changes to individual components of the proposed Plan may change the overall risk/reward profile of the PBR Plan for customers or the Companies (or both). Mr. Swanson elaborated:

> You know, as you pull on these individual components and, you know, you change a component in a plan without changing the compensating component in the plan, you really tend to, you know, shift risk in the plan in an asymmetrical way towards the company. And you know, along with that shift in risk you could run into a situation where it starts to impact return, right? And maybe the allowed return may have to be looked at if the shift in risk is significant.
>
> We do have safety mechanisms inherent in the proposal, being the off-ramps. So if it were to go too far, you know, there is a safety mechanism that could kick in. But as you move down that path in any one area, you do increase the chance of failure for the PBR plan in total.[43]

35. The provisions of the PBR Plan are not immutable, but any changes must be balanced. PBR is about opening up new opportunities for FortisBC to identify savings, to the mutual benefit of customers and the Companies. It should not be treated as an opportunity to shift risks to the Companies -- a premise which seems to underlie some of the changes to the PBR Plan that have been recommended by intervener experts.

(b) Intervener Recommendations that Would Not Be Just and Reasonable

36. Each of Mr. Bell, Ms. Alexander, and Dr. Lowry made recommendations that, if adopted, would impair the ability of the FortisBC Utilities to earn a fair return. Notable recommendations that run afoul of the regulatory compact are summarized below.

- ***Mr. Bell's Opposition to Growth Factors and Reliance on Historic Costs:*** Mr. Bell, on behalf of BCPSO, advocated excluding from the formula for O&M and capital

[43] T3:524, ll.5-20 (Swanson).

a factor that would account for growth in FEI's and FBC's business.[44] Yet, there is ample evidence on the record that growth drives costs. Failing to account for recognized and understood costs in the design of the PBR (and, in particular, without some reduction in productivity factors to accommodate growth implicitly), would have the effect of impairing the Companies' opportunity to earn a fair return. FortisBC expands on this point later in Part 3.

- ***Ms. Alexander's SQI Recommendations:*** Ms. Alexander's two key SQI recommendations would be unjust and unreasonable for reasons detailed in Part 5 of this PBR Submission. Briefly:

  - Ms. Alexander maintained that the PBR should mandate higher service levels than exist presently, without adjusting the base rates to account for the additional cost that would be required to provide a higher level of service. If the Commission determines that a higher level of service is appropriate, it must account for the incremental costs in the base year costs. Deliberately setting rates that are deficient would be inconsistent with the requirement in section 59(5) to "yield a fair and reasonable compensation for the service provided by the utility".

  - Ms. Alexander also advocated significant mandatory penalties when SQIs are not met. This is problematic for two reasons. First, service quality can be influenced by factors wholly beyond the utilities' control, even where the utility is acting prudently. Second, penalties that are not logically connected to the utility's actions that caused the decline in the service levels are arbitrary. The overall effect is to deny recovery of prudently incurred costs and to impair FortisBC's opportunity to earn a fair return.

[44] Exhibit B2-26, Package of Materials for Cross-Examination of Mr. Bell, p.14 (FEI Exhibit C5-6, Bell Evidence, p.13, Q16).

- ***Dr. Lowry's I-X-Formula Imposes Unrealistic Expectations:*** Dr. Overcast assessed the practical implications of Dr. Lowry's I-X formula (an exercise that, significantly, Dr. Lowry never sought to perform),[45] correctly noting that "I – X is not just an academic debate….If the results of the application of a formula provide no opportunity for the utility to earn its allowed return there is no reasonable basis for adoption of the formula."[46] Dr. Overcast summarized the practical outcome of Dr. Lowry's formula as follows:

> The PEG formula produces a cumulative shortfall in O&M revenues and capital expenditures relative to forecasts of between $112 million and $129 million for FEI depending on the low or high construction cost case and $34 million for FBC. These values are up to four and a half times as large as the required savings under the Companies PBR Plan. In other words, the PEG formula would require that the Companies achieve over four times the efficiency savings than those already proposed by the Company.[47]

Dr. Overcast characterized the efficiencies implied by Dr. Lowry's formula as being "substantially larger than you could reasonably expect for a company who'd been in PBR for as many years as these two companies have been in."[48] Dr. Overcast also noted that the impact on the shareholder of the shortfall is even larger than the difference based on total dollars might suggest because it all comes out of earnings.[49]

The reasons why Dr. Lowry's recommended I-X formula results in a revenue trajectory that is insufficient to meet the just and reasonable standard relate primarily to a significant upward bias in his estimated Total Factor Productivity

---

[45] See the PEG response, FEI Exhibit C1-13-1, BCUC-CEC IR 1.23.1.

[46] Exhibit B-45, Overcast Rebuttal Evidence, p.3.

[47] Exhibit B-45, Overcast Rebuttal Evidence, p.3.

[48] T3:515, ll. 3-11 (Overcast). Dr. Lowry himself acknowledged that utilities that have been under PBR for an extended period of time will have diminished opportunities to identify incremental savings: FBC Exhibit C6-13, BCSEA-CEC (Lowry) IR 1.7.1.

[49] T3:516, l.20-517, l.2 (Overcast).

("TFP") for the electric and gas industries. This topic is canvassed extensively in Part 4 of this PBR Submission. For now, it is sufficient to state that an X-Factor of this magnitude could be expected to present a material asymmetrical risk for the Companies that is not reflected in the allowed equity return.[50]

D. BUILDING ON PAST EXPERIENCE WITH PBR

37. FEI has been under PBR for 10 of the last 15 years.[51] FBC has been under PBR for 14 of the last 17 years.[52] Building on this past experience maximizes the potential for the Plan to deliver benefits to the Companies and customers. There is no justification to import PBR mechanisms from Alberta, as advocated by Mr. Bell.

38. Table B6-10 of the FEI Application[53] provides a side-by-side comparison of the FEI 2004 PBR Plan and proposed PBR Plan. The corresponding comparison to the 2007 FBC PBR Plan is in Table B6-9 of the FBC Application.[54] Although there were some specific differences between the prior plans of FEI and FBC, they shared overarching similarities. They both included an I-X formula based on a revenue cap design. They both excluded "lumpy" capital from the formula, and employed flow-through treatment for uncontrollable costs. There was symmetrical earnings sharing. The plans specified SQIs to ensure that the Companies did not compromise service quality for the purpose of increasing short-term earnings. The plans also included off-ramps in the event of unforeseen circumstances. In light of FBC and FEI being brought under common management, there is value to customers and the Companies to maximizing the potential symmetry between of FEI and FBC under a single PBR Plan.

39. Dr. Overcast's study of PBR plans in other Canadian jurisdictions supports building on a familiar and proven BC approach, rather than trying to import models wholesale

---

[50] T3:427, ll.12-26 (Overcast).

[51] 1998-2001 and 2004-2009.

[52] 1996-2004 and 2007-2011.

[53] FEI Exhibit B-1, FEI Application, pp.80-81.

[54] FBC Exhibit B-1, FBC Application, pp.73-74.

that were developed in a different context. While there are a variety of PBR methodologies, all are variants on the I-X concept that has been used by FortisBC in the past and in the proposed PBR Plan. Within that general I-X framework, each jurisdiction is tailoring the plans to fit its specific circumstances.[55] Ontario has different plans for different types of utilities. Dr. Overcast concluded that there is no one "right" PBR model, and that the framework adopted for the Companies should be in keeping with their specific circumstances.

40. Mr. Bell expresses the view that "if the Commission wants to create additional incentives to create innovation, then the Commission should consider alternative models such as price cap or revenue requirement per customer caps."[56] These are the types of plans in use in Alberta (the former is generally applied to electric utilities with only distribution functions, and the latter is generally applied to gas utilities with only distribution functions). The Commission should reject Mr. Bell's recommendation for two reasons.

- First, Mr. Bell appears to be concerned ultimately with the fact that FortisBC's proposal excludes costs from the formula, and is contrasting FortisBC's proposal with an idealized version of the AUC formulas.
    - The AUC has had to approve significant capital trackers for utilities in recognition that the formula would preclude utilities from undertaking necessary infrastructure investments. For instance, only 20% of EPCOR's 2013 capital requirements remained subject to the AUC's formula after the approval of a capital tracker,[57] which is significantly less than is contemplated under FortisBC's proposed PBR Plan. Dr. Overcast observed that a pure price cap or revenue cap formula that does not exclude some capital is unlikely to be practical.[58]

[55] A summary of conclusions from the jurisdictional study is included in FEI Exhibit B-1, FEI Application, p.42.
[56] FEI Exhibit C5-6, Bell Evidence, p.12.
[57] FEI Exhibit C5-6, Bell Evidence, p.7.
[58] FEI Exhibit B-1, FEI Application, p.33.

- Although uncontrollable costs are included within the formula in Alberta, the design of the Alberta plan leaves utilities with significant flexibility to accommodate them within the formula. The AUC plan, in effect, inflates (or applies the I-X formula to) the entire revenue requirement, including the cost of capital and the rate base in existence at the outset of the plan (as opposed to just applying the I-X formula to the additions to the rate base under the FortisBC Plan). Since the opening rate base will only decline over the PBR period (as assets are retired, the associated depreciation expense drops off and as assets are depreciated, their rate base value declines and the associated return on rate base decreases), this provides the Alberta utilities with significant room within the formula for new spending and to accommodate fluctuations in the costs of uncontrollable items. In contrast, the FortisBC plan flows these savings one hundred percent to customers over the PBR term.[59] Dr. Overcast stated that the buffer created by depreciation expense under the AUC plan "can be pretty significant numbers". He elaborated:

> I mean, if you think about what the annual depreciation expense is, that it's included in the revenue requirement, if you don't spend enough on capital -- you know, if you don't spend as much as the depreciation expense, all those dollars are available to you. Plus you are actually inflating the return component.
>
> So it's a very different plan and the conclusions that apply under the Alberta plan just don't even match up with what you're -- with the proposal you have before you.[60]

[59] Exhibit B2-8, BCUC-FEI/FBC IR 3.51.3 shows that for FEI the combined cost of debt and equity on existing assets declines by $38.2 million from 2014 to 2018. FBC Exhibit B-7, BCUC-FBC IR 1.21.1 shows that the combined cost of debt and equity on existing assets declines by $13.6 million during the same period. These savings are all flowed through to customers under FortisBC's PBR proposal.

[60] T4:816, l.19-817, l.4 (Overcast).

- Second, price caps and revenue per customer caps are less appropriate for vertically integrated utilities like FBC (transmission, distribution and billing/ customer care components) and FEI (transmission, distribution, storage, and billing/customer care components) than the essentially pure distribution utilities that are subject to the Alberta generic PBR.[61] Mr. Bell did not present any evidence to demonstrate whether and how a price cap model would work when applied to FortisBC. There are, for instance, known issues with price caps when applied to utilities with declining use per customer.[62] Dr. Overcast also identified other theoretical and practical issues with aspects of the plans developed in other jurisdictions that do not exist with the model being proposed by FortisBC.[63]

41. FortisBC's Rebuttal Evidence to Mr. Bell provided a good summary about how the components of the Companies' proposed PBR Plan act together to provide enhanced efficiency incentives for controllable costs, while retaining appropriate cost of service treatment for some items.[64] The Commission need only look to the long history of success in BC for confirmation that basing the PBR on the recent FEI and FBC plans is best approach going forward.

---

[61] Exhibit B-44, FortisBC Rebuttal to Bell, pp.9-10; FEI Exhibit C5-13, FEI/FBC-BCPSO (Bell) IR 1.2.1., 1.2.2.

[62] T3:430, ll.2-11 (Overcast); T3:472, ll.5-11 (Roy).

[63] FEI Exhibit B-1, FEI Application, p.27; FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada.

[64] FEI Exhibit B-44, pp.1-2. FortisBC was rebutting Mr. Bell's opinion that "the incentives in the building block model are not significantly different than cost of service regulation".

PART THREE: EVIDENCE ON COMPONENTS OF OVERALL PBR PLAN

42. In this Part, the Companies address the evidence on individual components of the PBR Plan other than the I-X formula and SQIs, which are addressed in Parts Four and Five, respectively. FortisBC makes the following points:

- A fixed five-year term is appropriate in the context of the overall PBR Plan.
- FortisBC's proposed cost treatment appropriately focusses incentives on controllable expenditures.
- FortisBC's symmetrical Earnings Sharing Mechanism ("ESM") brings greater alignment between the interests of customers and the Companies.
- The Efficiency Carry-over Mechanism ("ECM") strengthens the incentive to pursue efficiency initiatives throughout the PBR term, to the mutual benefit of customers and the Companies.
- The Mid-Term Review and off-ramps provide appropriate safeguards in the context of the overall PBR Plan.
- The Annual Review process is an appropriate mechanism for re-setting rates and for communicating with stakeholders about the Companies' performance under PBR.

A. A FIVE-YEAR TERM IS APPROPRIATE

43. FortisBC submits that a fixed five-year PBR term, effective 2014 to 2018, is appropriate in this case for the reasons described below.[65]

[65] FBC Exhibit B-15, ICG-FBC IR 1.5.2; FBC Exhibit B-10, CEC-FBC IR 1.3.1; T2:310, ll. 4-15 (Swanson).

44. A five-year term strikes an appropriate balance between achieving the objectives of PBR and regulatory oversight for three reasons:

- First, a five-year term is long enough to eliminate the need for at least one comprehensive revenue requirements application for each utility. This will bring significant direct savings, and internal resources that would have been occupied with preparing the revenue requirement application will be freed-up to focus on managing the Companies efficiently.

- Second, Dr. Overcast explained that "the term actually sets the economics for finding efficiencies" because the pay-back period for any investment in incremental efficiencies must be less than the time until rebasing occurs. A longer term opens up more opportunities for savings.[66] The types of efficiency investments identified under PBR generally require a few years for the benefits to be realized.[67] As it is, a five year plan will only provide the utilities with four and a quarter years to work with, given that the Commission's decision will be issued over half-way through 2014. This is not a lot of time to earn a payback on incremental efficiency investments.[68] The break-even on FEI's efficiency investments in the 1998-2001 PBR did not occur until the fourth and last year of the plan.[69] Mr. Swanson confirmed that a plan term of less than five years would require consideration of a downward adjustment in the X-Factor, explaining:

> At the beginning of a PBR term, we might not be able to get to the X factor right away. I think Ms. Roy had spoke to this earlier, where we might have to ramp up and by the end of the term

---

66 T2:262, l.23-263, l.12 (Overcast).

67 FEI Exhibit B-1, FEI Application, p.45.

68 T2:310, ll. 9-19 (Swanson). See also: FBC Exhibit B-10, CEC-FBC IR 1.3.1; FBC Exhibit B-15, ICG-FBC IR 1.5.2.

69 FEI Exhibit B-1, FEI Application, p. 45. FEI had actually required an extension of one year from an initial three year plan because "we were not able to actually recover our -- in that case some restructuring costs and that we actually needed the extension to actually finish recovering those restructuring costs." (T3: 537, ll.8-16 (Perttula))

> average that X factor. As you shorten the period, it leaves less opportunity to get there and achieve those X factors.[70]

- Third, any potential risks of a five-year PBR for either the utility or its customers are mitigated through other plan provisions such as the treatment of exogenous factors, SQIs, the Mid-term Review, and off-ramps. The Annual Reviews provide transparency.

45. Dr. Overcast confirmed at the hearing that he is "convinced that five years balances things in a reasonable way for all the participants", having regard to the other elements of the proposed PBR Plan.[71] He summarized his reasoning as follows:

> While there are reasons for selecting both shorter and longer periods, it seems that a five year period has become the most common period for review of PBR plans. From a theoretical view, the period must be long enough to permit the utility to earn the expected return on new cost saving technologies and not so long as to permit significant gains or losses for stakeholders. For a well developed plan that includes appropriate plan elements to preserve the fundamental regulatory compact for all stakeholders the five year period seems to be appropriate. The length of the plan must be set in conjunction with off-ramps and reopeners that protect all stakeholders. Further, the plan incentives must be symmetric and reasonable as will be discussed below. Shorter plans have a larger regulatory burden than longer plans in terms of the rate reset frequency. Longer plans have potentially lower regulatory costs but greater uncertainty of outcomes for stakeholders. The five year plan seems to be reasonable so long as other portions of the plan are reasonable. [72]

46. Participants raised the possibility of having no fixed term. A pre-determined, or fixed, term is vital to the success of the PBR Plan. The incentive power of a PBR plan comes, in part, from the utility having the certainty that it will have a longer period to recover incremental investments in achieving efficiencies.[73] Dr. Overcast identified that, without a pre-

---

[70] T3:535, ll.16-22 (Swanson).

[71] T3:541, ll. 2-13 (Overcast); FEI Exhibit B-1, FEI Application, pp.45-46.

[72] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.36.

[73] As Dr. Overcast noted: "If you only have one year, you're limited to efficiency investments that have a payback less than one year. If you have a five-year PBR plan, your set of potential incentives expands from those with a

determined PBR term, there is significant risk to the utilities in making such investments.[74] The risk to the Companies that the benefits could be re-based before payback is achieved would deter FortisBC from making investments beyond what it was compelled to achieve by the X-Factor, which undermines the whole point of PBR.[75] Moreover, combining an uncertain term with a significant X-Factor would put the Companies in an impossible position: they would have to invest to achieve significant incremental efficiencies with a real risk of losing money on those investments simply by virtue of a subsequent decision to rebase. This would present a significant asymmetric risk that was not contemplated in the Generic Cost of Capital Proceeding in setting these utilities' capital structure and ROE.

47. The Companies were asked for their views on an optional extension to the PBR Plan beyond 2018. The main benefit of a PBR plan extension would be to enable the utility to continue to pursue efficiency gains in the targeted areas (i.e. O&M and capital expenditures) over a longer period. The Companies would support a one-year term extension that would restore the full five-year period that has, by reason of the timeline of this process, been shortened by about 2/3 of a year. Other PBR Plan elements could remain unchanged with a one-year extension, since the PBR Plan was originally designed on that basis. However, a term extension beyond one year would represent a material modification to the overall PBR Plan proposal. A longer extension might well be beneficial for all stakeholders, and FortisBC is not opposed to it in principle;[76] however, the potential benefits come with some risk.[77] A longer extension should only be considered in the context of the other provisions of the PBR Plan. It may be appropriate to defer consideration of any additional extension beyond one year as part of the Mid-term Review, once parties have had some experience with the PBR Plan.[78]

---

one-year payback to those with a five-year payback. And obviously the second set is larger than the first set." (T2:342, l. 21-343, l.2 (Overcast))

[74] FEI Exhibit B-8, CEC-FEI (Overcast) IR 1.33.1.

[75] Exhibit B2-11, CEC-FEI/FBC IR 3.4.1; FEI Exhibit B-8, CEC-FEI (Overcast) IR 1.33.1; T2: 232, ll. 2-5 (Swanson).

[76] T3:555, l.18-556, l.8 (Swanson).

[77] T3:541, ll. 2-13 (Overcast).

[78] FEI Exhibit B-11, BCUC-FEI IR 1.3.1; FBC Exhibit B-7, BCUC-FBC IR 1.11.1; Exhibit B2-11, CEC-FEI/FBC IRs 3.6.1 and 3.6.2.

B. TREATMENT OF COSTS UNDER PBR PLAN

48. This section addresses how FEI's and FBC's rates will be determined under PBR, including the treatment of capital and O&M, flow-through items, CPCNs, limited rebasing and exogenous factors. FortisBC's proposal (apart from limited rebasing) reflects the treatment under FEI's prior plan and generally aligns with FBC's prior plan as well. FortisBC submits that focussing PBR incentives on regular controllable expenditures continues to make sense. The same rationale that supports flow-through treatment for non-controllable expenditures under cost of service regulation continues to apply under PBR.

(a) Overview

49. In essence, controllable costs for both Companies will be adjusted annually by the PBR (I-X) formula. The Companies will attempt to meet, and ideally incur costs below, those amounts in each year, with net savings greater than required by the formula to be shared according to the proposed Earnings Sharing Mechanism as those savings increase earnings. Other items will be re-forecast annually as part of the Annual Review process.

50. O&M expenses and capital expenditures are the two main types of controllable costs that present an opportunity for the Companies to identify and achieve cost savings. O&M and capital costs are treated separately, rather than considering total expenditures altogether under a single I-X formula. This approach (referred to as a "building-block" approach) has precedent in the prior approved FEI PBR plans as well as other plans and proposals in other jurisdictions. It provides a good framework for determining the allowed capital and operating costs for each year during the term along with the other adjustments for growth. It improves the ability of the formula to reflect the most relevant cost drivers. Moreover, the building block approach is more transparent since the Commission, by virtue of approving the O&M and capital formulas, also approves the allocation of costs between capital and O&M.[79]

[79] FEI Exhibit B-11, BCUC-FEI IR 1.15.1; FBC Exhibit B-7, BCUC-FBC IR 1.25.1.

(b) Controllable Costs – O&M

51. The general framework for treatment of O&M will be the same for both utilities. Actual O&M expenditures will not flow through to rates. Instead, the controllable O&M subject to the I-X formula will be escalated each year in the Annual Review, recalculated based on both the re-forecasted number of customers and the re-forecasted composite inflation rate for the upcoming year. The X-Factor will remain constant throughout the PBR Period,[80] which will incent the pursuit of further efficiencies in O&M expenditures.[81] FortisBC makes the following points below:

- FortisBC has included appropriate O&M under the I-X formula;
- It is reasonable to account for growth by adjusting O&M to reflect the average number of customers; and
- Mr. Bell's objections to incorporating a growth factor in the O&M formula (or capital formulae) are without merit and are inconsistent with the Companies' opportunity to earn a fair return.

Appropriate O&M Made Subject to the Formula

52. Consistent with the PBR Principles outlined in Part 2 of this PBR Submission, the O&M formula focusses on controllable costs. Certain non-controllable O&M is excluded from the I-X formula:

- ***Excluded for FEI***: Excluded from the O&M formula approach are pensions and OPEBs, insurance and also the O&M related to NGT Stations, Rate Schedules 16 and 46, and Biomethane. The pensions, OPEBs and insurance were also excluded from the formula in the last PBR and were considered flow-through items in recognition of their uncontrollable nature. The Rate Schedules 16 and

[80] FEI Exhibit B-1, FEI Application, pp.56-57; T4:715, l.1-716, l.1 (Roy).
[81] FEI Exhibit B-1, FEI Application, p.54.

46 O&M was excluded because these costs are directly tied to incremental revenue that is not part of the formula approach. The Biomethane O&M is not recovered through the delivery rate, but rather through a separate rate setting process.[82]

- ***Excluded for FBC:*** Excluded from the O&M formula approach are pensions and OPEBs, insurance, and the O&M related to implementation of the AMI Project. The pensions and OPEBs were excluded from the formula in the 2007 PBR. They were considered flow-through items due to their recognized uncontrollable nature. FBC is also requesting flow-through treatment and exclusion from the PBR formula for insurance expense,[83] for the same reasons articulated for FEI. AMI-related costs and reductions are excluded from the formula as the expenditure/savings profile is highly variable during the implementation period.[84]

Using Average Customers to Account for Growth in the Business

53. The I-X formula itself does not account for growth in the business. It is necessary to account for growth separately. As in the 2004 FEI PBR Plan and the 2007 FBC PBR Plan, the PBR formula applicable to O&M for both Companies will be tied to the average number of customers. The Companies will reforecast the average number of customers for the upcoming year in the Annual Review.[85] This process effectively adds an estimate of additional O&M expense associated with system growth to the PBR Plan's I-X revenue adjustment.[86]

---

[82] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, p.56.

[83] See FBC Exhibit B-1, FBC Application, p.263.

[84] FBC Exhibit B-1, FBC Application, p.52. Given that there are no O&M impacts in 2013 related to the AMI project, the 2013 O&M base amount applicable to the proposed PBR formula appropriately does not include any impacts related to AMI (as there are none). However, the O&M impacts (savings from 2015 onwards) are added back to the total O&M under PBR, thus ensuring that rates determined under the proposed PBR reflect the full benefit to customers attributable to the AMI Project. If the forecast O&M reductions from AMI change over the course of the PBR plan, then FortisBC would update its forecast: FBC Exhibit B-7, BCUC-FBC IR 1.30.1.

[85] FEI Exhibit B-1, FEI Application, p.56; FEI Exhibit B-11, BCUC-FEI IR 1.16.1; FBC Exhibit B-7, BCUC-FBC IR 1.26.1.

[86] FBC Exhibit B-1, FBC Application, p.53; FBC Exhibit B-7, BCUC-FBC IR 1.27.1.

54. There are two reasons why it is reasonable to use customers to account for growth in the context of O&M. First, adding customers directly impacts O&M. Costs for billing and meter reading are directly correlated to customer count and will increase as customer count grows. Costs for transmission and distribution operations and maintenance are indirectly related to customer count and will incrementally increase as customer and customer capacity requirements grow. The additions of pipeline and system capacity are lumpy investments that are required as existing capacity is fully utilized or as the existing gas plant reaches its end of life and must be replaced.[87] The same principle holds true for the electric system. Second, Dr. Overcast explained that although capacity is also a principal driver for O&M costs, the influence of the capacity component on O&M costs is not easily measured and a growth adjustment reflecting capacity changes would not be transparent. Customer count can serve as a reasonable proxy for both capacity and customers for the O&M adjustment.[88]

55. Issues were raised as to whether the customer count needs to be adjusted for excess capacity or inactive services. Dr. Overcast explained why the average number of customers used in the O&M formula should not be adjusted to reflect excess capacity:

> ...The O&M is a function of the pipe in the ground. For example, it doesn't matter if your design day capacity is 100 units for a section of pipe. It's that section of pipe that has to be maintained regardless of how much use is on the pipe. So you have to do a leak survey. You have to do any maintenance or any repairs to that pipe. So those things are not related to the capacity but more related to the miles of line or the type of pipe, where it's located.[89]

Inactive services are not reflected in the customer count, and thus do not affect O&M growth adjustments.

---

[87] FEI Exhibit B-8, CEC-FEI IR 1.42.1.

[88] FEI Exhibit B-1, FEI Application, p.56; FBC Exhibit B-7, BCUC-FBC (Overcast) IR 1.27.2.2 provides a lengthy explanation.

[89] T4:724, l.16-725, l.15 (Overcast).

Mr. Bell's Opposition to Growth Factors and Reliance on Historic Costs

56. Mr. Bell, on behalf of BCPSO, advocated excluding from the formula O&M and capital a factor that would account for growth in FEI's and FBC's businesses. His argument should be rejected.

57. There is ample evidence on the record that growth drives costs. In the course of a series of cross-examination questions, Mr. Bell also admitted that customer growth drives new capital investment and O&M for both electric and gas utilities, and that growth is not captured implicitly in the PBR Plan such that there would be no requirement for an explicit growth factor.

58. Mr. Bell's opposition to the inclusion of a growth factor appears to have been based on an incorrect assessment of FEI's and FBC's historic costs, and was influenced by a mistaken belief that growth is not accounted for in Alberta's PBR plan:

- In examining Mr. Bell's analysis, it becomes clear that he was only examining historic O&M costs on a per customer basis. Costs expressed on a per customer basis already account for changes in the number of customers, and cannot be used to derive any conclusions about whether or not there needs to be a growth factor reflected in the PBR Plan.[90]

- Although there are no explicit growth factors in the Alberta PBR formula, growth is captured implicitly.[91] The price cap and revenue cap per customer approaches in Alberta incorporate unit amounts that inflate with I-X and then are applied to delivery volume or number of customers. Growth can be left out of the price cap/revenue cap per customer formula since growth will be recovered from an increase in delivery volume or number of customers.

---

[90] Exhibit B-44, FortisBC Rebuttal to Bell, pp.2-3. FortisBC provided a numeric example.

[91] Exhibit B-44, FortisBC Rebuttal to Bell, pp.2-4. FortisBC explained how the linkage between customer growth and O&M cost increases is more direct for FortisBC than for the Alberta utilities to which Mr. Bell's PBR experience pertains because of the additional functions performed by FortisBC relative to the Alberta utilities.

59. The Commission has approved O&M formulas for FEI and FBC of the same or very similar nature dating back to the mid-1990s. While there have been refinements in the approved O&M formula over time, the same basic structure of O&M escalation from a base level based on customer growth and inflation less a productivity factor has been used in numerous PBR and revenue requirement applications since then.[92] Changing the O&M formula by removing growth, as advocated by Mr. Bell, is tantamount to increasing the productivity improvement requirements imposed on the Companies. FortisBC's proposed X-Factor of 0.5% already includes a significant stretch factor. Failing to account for recognized and understood costs in the design of the PBR, other things equal, would have the effect of impairing the Companies' opportunity to earn a fair return. It is most appropriate and transparent to account for growth explicitly, consistent with the previous PBR plans and as FortisBC has proposed here.

(c) Controllable Costs – Capital

60. The treatment of capital under the PBR Plan is addressed in section B6.2.6 and B6.2.5 of the FBC and FEI Applications, respectively. This is one area where there is a difference in how the PBR Plan formula is calculated for FEI and FBC, and it is attributable to the different nature of capital costs for gas and electric systems. In both cases, the capital formulae appropriately:

- focus on the main component of rate base over which FortisBC has the greatest degree of control;[93] and
- account for the drivers of growth, sustainment and other capital.

Capital Included Within the I-X Formula

61. As proposed, three categories of regular capital – growth, sustainment and other capital – will be subject to the I-X mechanism for both Companies.[94] Actual regular capital

[92] Exhibit B-44, FortisBC Rebuttal to Bell, p.4.

[93] FEI Exhibit B-1, FEI Application, p.59; FBC Exhibit B-1, FBC Application, p.54.

[94] FEI Exhibit B-11, BCUC-FEI IR 1.17.1; FBC Exhibit B-7, BCUC-FBC IR 1.31.1.

expenditures and resulting plant additions will not be flowed through in rates. The formula-based capital expenditures for the upcoming year will be recalculated in each Annual Review. They will then be added to rate base and included in rate calculations through the PBR term. Regular growth capital and sustainment and other capital are included under the formula because the required spending on these types of capital can be accommodated under a formula, and the costs can be influenced by the Companies. The categories of capital that fall outside of the I-X mechanism, and the rationale for their exclusion, are discussed in the Applications/Evidentiary Updates.[95]

FEI's Approach Reflects Drivers of its Growth and Sustainment Capital

62. FEI proposes to apply one I-X formula to growth capital and another to sustainment and other capital. A description of the types of capital included in each of these categories is included in Section C5 of the FEI Application. It is appropriate in the case of FEI to use two different formulae because each category of capital has different cost drivers:

- ***Growth Capital:*** FEI's growth capital is primarily driven by customer additions - more specifically, by service line additions that arise from providing service for new customers. FEI has adopted as the appropriate cost driver for growth capital the number of customers for whom a service line is added, calculated as 90% of gross customer additions (where the forecast of customers is the same as used in FEI's demand forecasts and the percentage reflects the actual ratio recently experienced).[96]

- ***Sustainment/Other:*** Sustainment capital pertains to capital work required to sustain the system for all customers (existing and new). FEI's sustainment capital

---

[95] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, p. 61; FBC Exhibit B-1-6, FBC Application Evidentiary Update October 18, 2013, p.57.

[96] FEI Exhibit B-6, BCPSO-FEI IR 1.21.3; see also Exhibit B2-10, BCSEA-FEI/FBC IR 3.1 series; T4:726, ll.1-4 (Overcast). Dr. Lowry's notion that this gives rise to opportunities to "game the system" by adding unused service lines is absurd on its face and in any event those would not be picked up in the count: T4:699, l.10-700, l.3 (Overcast, Roy). The annual re-determination of growth capital is outlined in FEI Exhibit B-6, BCPSO-FEI IRs 1.20.1 and 1.20.2.

costs are actually driven by both capacity and customers, but developing a capacity measure for adjusting capital suffers from the challenges previously described in the context of O&M. The customer driver is a reasonable proxy for the sustainment capital spending because it recognizes that as more customers are added to the system, the overall size of the system will increase. More capital of a sustaining nature is needed to serve the larger system.[97] FEI explained, for instance:

> Sustainment capital includes the installation of system capacity improvements. System capacity improvements are required when a significant number of additional customers connect to the system and the forecasted pressures within the piping system will be too low to provide adequate gas supply to all customers and generally take the form of the installation of additional mains in parallel with the existing mains. Thus, customer growth within a piping system drives the need for system capacity improvements and sustainment capital expenditures.[98]

FEI has thus adopted average customer count as the appropriate cost driver for capital spending in this category. The customer count represents the meters that are actually providing service to live customers, and does not include inactive meters.[99]

Apart from the use of forecast service line additions instead of forecast customer additions, FEI's proposed capital formulae are conceptually identical to the formulae in the 2004 FEI PBR.[100] Dr. Overcast characterized the change to the growth capital driver as "the most conservative way to increase the capital".[101]

---

[97] FEI Exhibit B-1, FEI Application, pp.63-65; T4:697, l.24-698, l.12 (Roy).

[98] FEI Exhibit B-6, BCPSO-FEI IRs 1.21.2 and 1.21.3; with respect to FBC, see FBC Exhibit B-11, BCPSO-FBC IR 1.43.2.

[99] FEI Exhibit B-6, BCPSO-FEI IR 1.21.3; see also Exhibit B2-10, BCSEA-FEI/FBC IR 3.1.1; T4:728: ll.14-16 (Roy).

[100] Exhibit B-44, FortisBC Rebuttal to Bell, p.5, ll.36-40.

[101] T4:700, ll.4-15 (Overcast).

63. Treating all of FEI's capital subject to the PBR I-X formula in one category would fail to recognize key cost driver differences between growth capital and the sustainment/other categories. Growth capital is ultimately driven by requests from developers or potential customers to attach to the gas system and the level of growth varies for numerous reasons. In contrast, with sustainment and other capital FEI has some flexibility to manage the timing of projects. A single formula encompassing all capital, inclusive of growth capital, would give positive or negative variances for inappropriate reasons.[102]

FBC's Single Capital Formula Appropriately Reflects its Capital Cost Drivers

64. FBC is proposing to use a single formula for regular growth and sustainment and other capital. Relative to a gas utility, there is less need in the case of an electric utility to have a separate formula for growth capital. Electric growth capital is driven more by overall system size (and changes in overall system size) than it is for a gas utility. System capacity constraints are more of an issue for electric infrastructure. Since it is difficult to develop a transparent way to adjust FBC's capital for changes in capacity, FBC has proposed a capital formula using changes in total customer count as a reasonable proxy for the capacity variable in the formula.[103]

Variances from Forecasts

65. The issue raised at the hearing of the potential for there to be variances from the forecasts used to determine growth is, in fact, not a significant issue. First, FortisBC is using the same customer forecasting methodology as it always uses, and that has a proven track record.[104] Second, the number is re-forecast every year based on updated numbers.[105] Third, the growth component in the formulae is less than 1% per year (based on the forecast customer growth).[106] Even in the case of a "large" variance in the forecast, "we're talking about

---

[102] FEI Exhibit B-11, BCUC-FEI IRs 1.19.1 and 1.19.1.1.

[103] FBC Exhibit B-1, FBC Application, pp.56-57.

[104] T4:699, ll.21-25 (Roy).

[105] T4:702, ll.11-25 (Roy).

[106] Exhibit B-44, FortisBC Rebuttal to Bell, p.5.

numbers like the difference between .6 and 2. It's not like we're going to get into situations where we have 5 percent customer growth or anything of that order of magnitude."[107] FortisBC submits that the proposed methodology for accounting for growth is reasonable and should be accepted.

(d) Limited Rebasing of Capital

66. The Companies proposed limited rebasing of capital if capital expenditures are below 90% or above 110% of the formula-based amount for the year.[108] In essence, "if the capital spending is outside of a band of 90 percent to 110 percent of the formula amount in any given year, then the re-basing will be for that amount that exceeds that on either side."[109] The Companies are ambivalent about whether there should be limited rebasing in the PBR Plan at all, given the pros and cons. If limited rebasing is to be adopted, a band of +/- 10% represents the appropriate balance among competing objectives.

67. FortisBC proposed limited rebasing of capital costs to address the concerns of some interveners in prior proceedings regarding the deferral of expenditures beyond the PBR term.[110] Limited rebasing does provide customers with some assurance in that regard, in the sense of limiting the potential earnings from capital savings. At the same time, however, annual recalibration of capital expenditures decreases in the incentive power of PBR plans because it discourages investments that will reduce capital above the point where rebasing occurs.[111] It can also increase the regulatory burden to all stakeholders since limited rebasing adds complexity to the Annual Review process.

---

[107] T4:702, l.26-703, l.5 (Swanson). This is true even considering the effect of incorporating FEVI: T4:705, ll.4-8 (Roy).

[108] FBC Exhibit B-10, CEC-FBC IR 1.27.1. Capital spending below 90% of the formula-based amount in any year will lead to a reduction to opening rate base for ratemaking for the following year while capital spending above 110% of the formula-based amount in any year will lead to an increase in opening rate base for ratemaking for the following year.

[109] T3:493, ll.10-16 (Perttula); FEI Exhibit B-1-1, FEI Application, Appendix D4, p.3.

[110] Exhibit B2-8, BCUC-FEI/FBC IR 3.12.5; T4:706, ll.1-7 (Roy).

[111] T3:493, ll.17-21 (Roy).

68. In the event that the Commission considers limited rebasing to be appropriate, it is important in defining the threshold to strike a balance between the specific objective of limited capital rebasing and the overall objectives of the PBR plan.[112] Mr. Swanson characterized the +/- 10% proposal as "a judgment call on how much protection versus how much incentive you want to provide. We looked at a ten percent variance as being a reasonable level of incentive to provide, as well as providing a bit of a safety net."[113]

69. The rationale for limiting any rebasing to +/- 10% becomes clear if one examines what that threshold represents in terms of capital savings. Assuming that FBC's proposed formula-based capital amounts remain unchanged, on an average annual basis, the 10% trigger will be reached if actual capital spending in the formula based categories varies by more than $4.6 million from the approved formula amounts. Mr. Swanson noted that this amount translates into a relatively small amount of earnings sharing: "…if you had a carrying cost factor of approximately 10 percent, that'd be a little less than half a million dollars of pre-tax. You'd then take your tax on that so you'd be down to 400,000ish, and you would share that 50/50. So the incentive would be approximately 200,000 on that 10 percent in that example, to give you an order of magnitude of the impact."[114] FBC believes that the proposal reflects an appropriate amount that may be achieved through efficiency improvement investments.

70. Threshold levels lower than 10% would significantly blunt the incentive power under the PBR Plan and diminish the potential incremental savings generated for customers and the Companies.[115] Dr. Overcast agreed that a 5 percent cap and limited rebasing "probably isn't sufficient to give you the best set of incentives."[116] Moreover, adopting a threshold below

[112] T3:495, l.22-496, l.20 (Overcast).
[113] T4:706, ll.20-26 (Swanson).
[114] T3:497, ll.6-17 (Swanson); Exhibit B2-8, BCUC-FEI/FBC IR 3.12.2.1.
[115] T3:495, ll.1-21 (Roy).
[116] T3:496, ll.7-12 (Overcast).

10% will put the capital component of the PBR plan at greater risk of turning into a complicated cost of service plan with the limited rebasing occurring on an annual basis.[117]

(e) Flow-Through Costs and Revenues (Y-Factors)

71. The flow-through revenue and expense items under the proposed PBR Plan (sometimes referred to as "Y-Factors") reflect known cost and revenue sources of uncertain quantum. They are listed and described in the Applications and elaborated on in a number of responses to IRs.[118] Flow-through mechanisms ensure that customers pay actual costs in circumstances where the Companies have little ability to influence the level of expenditures or revenues.[119] The deferral treatment of flow-through items is the same under the proposed PBR Plan as it is today under cost of service regulation, and the rationale for flow-through treatment is the same in both cases.

72. The vast majority of the flow-through costs (85%-90%) consist of power purchase costs for FBC and residential and commercial gas usage for FEI. Both of these items are already subject to deferral treatment today due to their uncontrollable nature. Ms. Roy summarized the other items as follows:

> And I think if you read that [response to CEC-FEI IR 1.46.1], it's fairly clear as to the fact that there's very little we can do to influence that. For example, interest expense driven by the underlying interest rates, which of course we can't control. Return on equity is set by the Commission. Property taxes are set by property tax assessment rates and assessable values of the property. Income taxes of course, income tax rates. Pensions and OPEB expenses, we have quite a bit in there on to why those items are flowed outside the formula because of the assumptions such as the discount rate, the expected return on plant assets, rate of inflation, number of employees that are retiring, rates of mortality. Insurance

---

[117] Exhibit B2-8, BCUC-FEI/FBC IR 3.12.2.1; also T3:495, l.22-496, l.20 (Overcast).

[118] FEI Exhibit B-1, FEI Application, pp.67-70; FBC Exhibit B-1, FBC Application, pp.60-63. See also, FEI Exhibit B-8, CEC-FEI IR 1.46.1. See also: FBC Exhibit B-10, CEC-FBC IRs 1.34 (interest expense), 1.35 (taxes), 1.36 (pension), 1.37 (power purchase), 1.38 (revenue), 1.39 (depreciation and amortization), and 1.40 (rate base other than plant); FBC Exhibit B-7, BCUC-FBC IR 1.36.1 (future MRS-related costs not in the base); Exhibit B2-11, CEC-FEI/FBC IR 3.23.3; T3:488, l.13-493, l.4 (Roy).

[119] FEI Exhibit B-1, FEI Application, p.67; FBC Exhibit B-1, FBC Application, p.60.

> costs are mainly driven by disaster, natural disasters and events outside of our control. So we have walked through those areas.[120]

73. FEI is not requesting any new deferral accounts in this Application specifically related to any of the flow-through items discussed in the PBR application. Existing deferral accounts that capture variances between the actual and forecasted costs will continue through the PBR period.[121] FBC is requesting some deferral accounts to ensure consistent treatment with FEI, which is important in trying to align the incentives under common management.[122]

74. Mr. Swanson observed that there has been a long history for both utilities that has led to uncontrollable costs being flowed through to customers using deferral accounts.[123] The Commission commented favourably on the use of deferral accounts for uncontrollable items in its decision on FBC's 2012-2013 RRA, in the context of approving a number of flow-through accounts including the power purchase and revenue deferral accounts: "In the Panel's view, the creation of these deferral accounts represents a reasonable attempt to manage the uncertainty and unpredictability associated with accounts which are largely uncontrollable in nature."[124]

75. The same rationale exists under PBR as under COS ratemaking for flowing-through these costs. Including non-controllable costs within the formula can result in a windfall to either customers or the Company, which is undesirable. Ms. Roy made this point at the hearing, stating that "PBR is not about passing on uncontrollable costs between customers and companies, it's about incenting efficiencies and controllable costs. So, in our view, there is no difference in the treatment of deferral accounts between cost of service and PBR.[125]

---

[120] T2:300, l.24-301, l.14 (Roy).

[121] FEI Exhibit B-6, BCPSO-FEI IR 1.22.1.

[122] FBC Exhibit B-1, FBC Application, pp.246, 258.

[123] T2:297, ll.10-13 (Swanson).

[124] *In the Matter of FortisBC Inc. 2012-2013 Revenue Requirements and Review of 2012 Integrated System Plan* Decision, Commission Order G-110-12, August 15, 2012 (the "FBC 2012-2013 RRA Decision"), p.115; T4:831, l.16-832, l.21 (Swanson).

[125] T4:811, ll.9-18 (Roy); Ms. Roy discussed flow-throughs in greater detail starting at T2:238, l.8.

76. Dr. Overcast endorsed flow-through treatment under PBR for the items identified by the Companies.[126] He noted that most PBR plans have clauses to address uncontrollable costs like commodity costs and pension adjustments.[127] He also identified that it is important to allow full recovery of these costs under a PBR plan, as the costs - being outside the control of management - are by definition prudently incurred costs of providing utility service that should be recovered from customers in the normal course.[128]

77. In summary, the proposed treatment is appropriate and should be approved.

(f) CPCN Capital Treated Outside Formula

78. FortisBC is proposing to exclude CPCN capital from the formula in the same manner as under the previous FEI PBR. CPCN expenditures will only be included in rate base after receiving CPCN approval from the Commission (likely in a separate hearing from the Annual Review) and being placed into service.[129] There are three key reasons why it is important to exclude CPCN capital:

- First, CPCN capital is "lumpy". These are large projects. They are more difficult to forecast, as they fall outside of regular capital and are typically "one-off" projects. There is no prospect, for instance, that FEI's estimated $220 million of CPCNs expected for the PBR period could be accommodated within the formula as proposed.[130] The alternative approach of reflecting some average of CPCN capital in the base and applying the formula to it would create a significant potential for the utility to obtain large windfall benefits. Ms. Roy provided an example of how such windfalls might occur:

[126] FEI Exhibit B-1, FEI Application, pp.67-68; FBC Exhibit B-1, FBC Application, pp.60-61.
[127] T4:838, l.23-839, l.22 (Overcast).
[128] FEI Exhibit B-1, FEI Application, pp.67-68; FBC Exhibit B-1, FBC Application, pp.60-61.
[129] T2:334, ll.21-24 (Roy).
[130] T3:529, ll.4-9 (Roy); T4:626, l.15-18 (Roy).

> We don't know today that we are actually going to do those CPCNs. We don't know the timing of the CPCNs, we don't know the amount of the CPCNs. They are very uncertain. And I think if you've been involved in our CPCN applications you can see things change as we go through and decisions change and, of course, estimates change.
>
> So what you would be doing effectively is providing this rather large envelope of spending which is only going to provide, in my opinion, potential for, you know, windfall gains or losses for the company. You know, I don't think it's a practical solution.[131]

Dr. Overcast pointed out that these windfalls can arise from prudent system planning because having an annual amount included in the formula for CPCN capital doesn't reflect how prudent system planning is done.[132]

- Second, providing the Companies with a large envelope of spending that may or may not materialize takes away the visibility that is one of the major benefits of the PBR Plan.

- Third, by including costs of projects that would meet the CPCN threshold under the formula, the Commission faces the choice of either having to grant the CPCN on the basis originally reflected in the base year, or allowing the utility to obtain a significant windfall from the savings associated with not undertaking the project.

79. As under the previous FEI PBR, the separate CPCN process is a safeguard to ensure that CPCN projects are accorded the appropriate level of scrutiny from the Commission and interveners and that only actual costs related to CPCN projects are included in rates.[133]

---

[131] T4:626, l.25-627, l.22 (Roy); T4:688, ll.17-26 (Roy).

[132] T4:632, l.15-635, l.19 (Overcast).

[133] T2:334, ll.11-18 (Roy); T3:492, ll.21-26 (Roy).

80. At the hearing, parties explored why it is that more lumpy capital can potentially be accommodated in the Alberta PBR plan formula. The AUC plan is fundamentally different in that it involves, in effect, inflating (i.e. applying the I-X formula to) the entire revenue requirement, including the cost of capital and the rate base in existence at the outset of the plan (as opposed to just inflating the additions to the rate base under the FortisBC PBR Plan). The opening rate base will only decline over the PBR period; as assets are retired, the associated depreciation expense drops off and as assets are depreciated the Alberta utility's rate base value declines and the associated return decreases. This provides the Alberta utilities significant room within the formula for new spending and to accommodate fluctuations in the costs of uncontrollable items. In contrast, the FortisBC plan flows these savings one hundred percent to the ratepayers over the PBR term.[134] Even then, the AUC has had to employ significant capital trackers to make it work for utilities with significant capital spending plans. 80% of EPCOR's capital was excluded from the formula in 2013. 44% of AltaGas' 2013 capital was included in a capital tracker.[135]

81. Attempting to include CPCN capital within the capital formula, whether by adjusting the base or increasing the CPCN threshold or otherwise, would represent a fundamental change to the proposed PBR Plan. The formulas "have been calibrated excluding those dollars".[136] Mr. Swanson agreed with Mr. Miller's suggestion that "We aren't talking about minor tweaking. It has -- we're talking about major redevelopment here."[137] Dr. Overcast was asked about the effect on the X-Factor of including "some CPCNs, of either category [growth or sustainment]…into base capital amounts". He walked through an illustrative calculation and indicated that "I'm absolutely certain it would be a large -- I mean a drop into

[134] T4:629, l.22-630, l.2 (Overcast)

[135] T4:640, l.2-641, l.6 (Roy, Overcast); T4:668, l.14-669, l.4 (Overcast).

[136] T4:650, ll. 3-17 (Perttula).

[137] T4:650, ll.18-24 (Swanson).

the negative range."[138] The significance of the change is underscored by FortisBC's response to Exhibit B2-25, Undertaking No. 9.

82. In summary, the most reasonable approach for the FortisBC Utilities is to exclude CPCN capital from the formula, consistent with FEI's last PBR plan.

(g) Exogenous (or "Z") Factors

83. In the nomenclature of PBR, unforeseeable costs or revenues that are flowed through to rates outside of the formula are referred to as exogenous factors or Z-Factors. Consistent with FEI's 2004 PBR Plan and FBC's 2007 PBR Plan, the Companies propose that during the term of the proposed PBR Plans, customers' rates will be adjusted for exogenous factors.[139] Exogenous or Z-Factor treatment of these costs will ensure that customers pay only for the actual costs in circumstances where the Companies do not control the level of expenditures.[140]

Nature of Exogenous Factors

84. The very nature of exogenous factors - i.e., unforeseen and uncontrollable - makes compiling a comprehensive list of potential factors impossible. They could be associated with additional costs, revenues or savings. The lists provided in the Applications are representative of the types of events that would constitute exogenous factors.[141] FortisBC elaborated on items in the list in various IR responses.[142] In the last FEI Plan, there were exogenous factor applications.[143] A number of those applications related to tax rate changes

---

[138] T4:648, l.17-649, l.26 (Overcast).

[139] FEI Exhibit B-1, FEI Application, p.70; FBC Exhibit B-1, FBC Application, p.63.

[140] FEI Exhibit B-1, FEI Application, p.70; FBC Exhibit B-1, FBC Application, p.63. For further discussion of the rationale for exogenous factor treatment, please refer to the B&V PBR Report (FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p. 7).

[141] Exhibit B2-11, CEC-FEI/FBC IR 3.29.1.

[142] Exhibit B2-8, BCUC-FEI/FBC IR 3.22 series.

[143] T4:804, l.13-805, l.4 (Swanson, Roy).

and favoured customers.[144] FBC had similar applications, the most notable of which was for MRS implementation.

85. Changes of this nature, if not flowed through as exogenous factors, would lead to windfall gains or losses for the Companies (or windfall gains and losses for customers).[145] The provision for exogenous factors would address similar factors that would be addressed under a COS regime through the use of deferral accounts pending the next revenue requirement application.[146] Dr. Overcast stated that it is typical in the context of PBRs to treat uncontrollable factors outside of the PBR formula, "particularly where the cost changes represent cost changes that would be passed through as part of a cost of service proceeding."[147]

Materiality is a Practical Consideration Not a Design Consideration

86. The Commission should not impose a materiality requirement on exogenous factor adjustments, an idea that was raised in information requests. The cost increases or decreases arising from exogenous factors are non-controllable costs, and are therefore prudent by definition. They would, without question, be recoverable in rates under cost of service-based ratemaking without any materiality threshold. Barring recovery of unforeseen, uncontrollable and prudently incurred costs would be no more valid under PBR.[148]

87. While, in principle, all unforeseen events that are beyond the Companies' control should be treated as exogenous, the Companies' evidence is that they may choose not to apply to recover amounts related to small events that do not have an impact on the

[144] T4:801, l.22-802, l.4 (Roy).

[145] Exhibit B2-11, CEC-FEI/FBC IR 3.25.1.

[146] T4:807, ll.4-13 (Roy).

[147] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.36.

[148] FEI Exhibit B-6, BCPSO-FEI IR 1.23.2; FBC Exhibit B-7, BCUC-FBC IR 1.38.1; FBC Exhibit B-11, BCPSO-FBC IR 1.45.2; FEI Exhibit B-11, BCUC-FEI IR 1.22.1; Exhibit B2-11, CEC-FEI/FBC IRs 3.22.3, 3.25.5, and 3.25.2.

Companies' ability to serve its customers and that do not have a material cost impact.[149] This is, in fact, what happened under past PBR plans. However, the decision not to apply for recovery of a small cost must be treated as a practical determination, appropriately made by the Companies at the time and not by the Commission in advance.

Process for Addressing Exogenous Factors

88. The Companies will keep the Commission and stakeholders apprised of exogenous events. The type of notification will depend on the extent, timing and circumstances of the exogenous factors. Some items such as changes in Generally Accepted Accounting Principles ("GAAP") or items that result from Commission Decisions will be provided within the Annual Review process. For other items, forms of notification may include letters to the Commission, and the Companies will include discussion of exogenous factors during each Annual Review process. It is not necessary, and is impractical, to be overly prescriptive in advance as to mechanisms for addressing exogenous factors. The Commission and stakeholders have dealt many times with the recovery of costs from Z-factor type events in utility rates and various mechanisms such as flow-throughs, deferral accounts, true-ups and others have been employed to accomplish this.[150]

C. EARNINGS SHARING MECHANISM

89. ESMs are a common feature in PBR generally.[151] FortisBC's proposed ESM, which is symmetrical in nature, is the same as the mechanism incorporated in both Companies' prior PBRs. It is a key mechanism under the proposed PBR Plan for bringing greater alignment between the interests of customers and the Companies.[152]

---

[149] Exhibit B2-11, CEC-FEI/FBC IRs 3.29.1.1 and 3.32.7.

[150] Details of how exogenous factors can be addressed procedurally are included in the responses to Exhibit B2-11, CEC-FEI/FBC IRs 3.29.7, 3.29.8 and 3.29.9.

[151] T2:240, ll.3-15 (Roy).

[152] FEI Exhibit B-1, FEI Application, pp.70-72; FBC Exhibit B-1, FBC Application, pp.64-65.

90. The proposed ESM contemplates equal sharing between customers and FortisBC during the PBR period for earnings above and below the allowed ROE established by the Commission. In essence, if the utility is able to generate savings in excess of the savings implicit in the 0.5% X-Factor, then customers receive 50% of the earnings benefits during the PBR period (and any efficiency carry-over period, discussed later). Customers then receive 100% of the benefits upon rebasing.

91. There is a strong theoretical rationale for adopting an ESM based on equal sharing between customers and the utility. Dr. Overcast explained that earnings sharing is based on assuring that an acceptable level of benefits are shared with consumers during the regulatory control period and that the utility is protected from unreasonably low returns in the event of unforeseen plan outcomes.[153] He commented as follows on FEI's previous 50/50 ESM, which was the same as the current proposal:

> The FEI plan included an earnings sharing mechanism that provided symmetric protection for all stakeholders. As a matter of regulatory policy, this reduces the risk of unfavorable outcomes for both FEI and stakeholders. Particularly, the ESM provided customers with real time benefits if FEI earned above the authorized return and assured customers that FEI would not be permitted to deteriorate financially such that system service, safety and reliability would not be compromised.[154]

The successful results of the past PBR plans reinforce the benefits of including an ESM in this PBR Plan.[155]

---

[153] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.37; FEI Exhibit B-8, CEC-FEI IR 1.48 series. In the absence of the ESM, all savings would accrue to the utility as would be the case under cost of service ratemaking. The shareholder would similarly bear the brunt of any under-earning, which adds risk.

[154] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.46.

[155] FEI Exhibit B-8, CEC-FEI IR 1.23.1; FBC Exhibit B-10, CEC-FBC IR 1.15.1.

D. EFFICIENCY CARRY-OVER MECHANISM

92. The 2004 FEI PBR included a mechanism that carried over benefits relating to capital savings beyond the term of the PBR.[156] The Companies have built on that concept in proposing a five-year Efficiency Carry-over Mechanism, or ECM, that incorporates both O&M and capital. FortisBC submits that the ECM is a valuable component of the PBR Plan that strengthens the incentive to pursue efficiency initiatives throughout the PBR term, to the mutual benefit of customers and the Companies.

(a) How the ECM Works

93. FortisBC described in detail, with examples, how the proposed ECM works in Commissioner Cote's undertaking from the procedural conference.[157] Reduced to its essence, the ECM is a simple concept. Mr. Swanson articulated its function as follows:

> Also in its simplest form, I mean, whenever you look at a mathematical formula, it can seem confusing to some people. But really all the ECM is doing in its simplest form, it says regardless of when the savings occur, they're shared 50/50 for five years. And that's all the math is doing. So it's ensuring that regardless, it doesn't matter if it happens on the first day of PBR or the last day of PBR, the sharing of that benefit between customer and shareholder simply occurs for five years. The rest is just math to accomplish. So the concept is not a complicated concept. The math, and you're looking at rollover every year, yeah, it looks a little bit complicated but it's really not nearly as complicated as it may seem.[158]

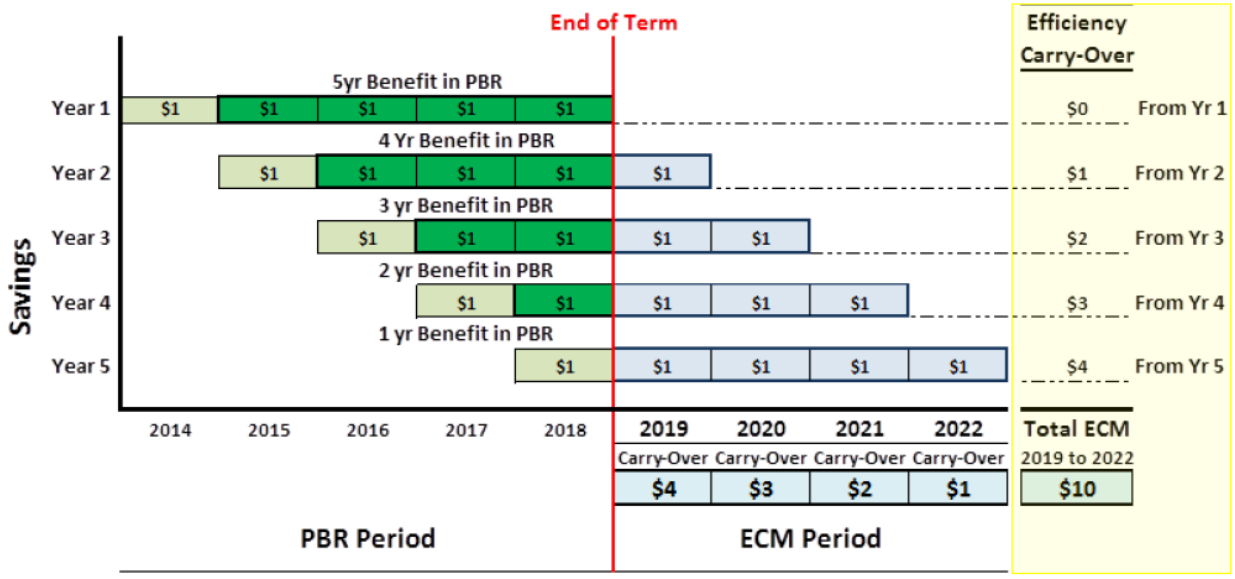
---

[156] The 2004 PBR Plan included an ECM under which the accumulated capital benefits at the end of the term were phased-out by declining factors of 2/3 in the first year after the plan expiry and 1/3 in the second year after: FEI Exhibit B-1, FEI Application, p.73.

[157] FEI Exhibit B-16; FBC Exhibit B-6.

[158] T2:308, ll.7-21 (Swanson).

94. An illustration of how the ECM achieves that straightforward principle was included in the following figure from the Panel 1 Opening Presentation:[159]



95. The example above is based on O&M and is indicative of a $2 savings from an efficiency gain at the beginning of each year of the PBR plan, for which $1 dollar is provided to customers and $1 is provided to the company. Total efficiency gains are measured as the variance between actual expenditures and formula-based forecasts on a year-to-year incremental basis to avoid rolling forward temporary savings. The company's share of the efficiency gain is carried forward for five years regardless of the year in which the savings were achieved. The customers' share results in a permanent decrease in the costs that make up rates going forward at the end of the PBR term.

96. For capital expenditure savings, only a small percentage of the capital savings - referred to as "the rate base benefit factor" - would be included in the ECM.[160]

97. The ECM calculation occurs only once at the end of the PBR period based on actual costs, not each year at the Annual Review.[161]

---

[159] FEI Exhibit B-48; Mr. Perttula walked through another example starting at T2:315, l.9 (Perttula).

[160] FEI Exhibit B-1, FEI Application, p.74; FBC Exhibit B-1, FBC Application, p.67.

(b) The Logic of an ECM

98. In the absence of an ECM, the incentive to invest in incremental savings declines throughout the PBR term. As time passes, the window during which the utility must achieve a payback on its investments gets smaller. An ECM addresses this issue by breaking the link between the timing of efficiency gains and the PBR incentives. It ensures that the stream of savings resulting from an investment in efficiencies will be allocated to help repay the investment regardless of how close the investment is to the end of the term of the PBR Plan. The ultimate benefit to customers is that the aggregate costs embedded in rates associated with a five-year PBR term plus ECM would be lower than they would be in the absence of an ECM.[162]

99. Including O&M in the ECM along with capital encourages FortisBC to seek the most efficient combination of these expenditure types throughout the PBR term. Mr. Swanson explained that the capital ECM is particularly integral to the overall PBR Plan.[163] Incorporating O&M was intended to address stakeholder concerns about O&M costs increasing towards the end of the period.

100. It appears, based on some of the questions on the ECM, that there is a perception that the ECM results in the utility obtaining a benefit for nothing. It is important to understand that the savings that are subject to the ECM are unlikely to have been generated in the absence of the ECM because the payback period would have been too short to make economic the necessary investments to generate the incremental savings. Dr. Overcast stated:

> When capital and other costs are rebased at the end of the control period all of the benefits from capital and savings on O&M immediately flow through to customers in lower rates. This means that investments in efficiency that have a longer payback period than the remaining time under the PBR plan would be

---

[161] T3:501, l.21-502, l.9 (Roy).

[162] T4:767, ll.14-20 (Overcast); T2:242, ll.7-10 (Roy); T4:756, ll.1-13 (Swanson); FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.38.

[163] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, p.67; T4:768, ll.2-23 (Swanson, Roy).

> discouraged because the utility could not expect a full payback on the investment before the savings were appropriated for customers.[164]

101. Mr. Swanson echoed these comments at the hearing, explaining that in the absence of an ECM "you would wait until your next cost of service application where you could forecast the costs and benefits associated with doing that initiative. So it delays the benefit."[165]

102. ECMs have been adopted in Alberta and for Gaz Metro.[166] The logic outlined above supports the inclusion of an ECM in the FortisBC PBR Plan.

(c) Potential Modification to Address Matter Identified by Commission Panel

103. In the course of the oral hearing, Commissioner MacMurchy explored the potential of modifying FortisBC's proposed ECM so that "no benefits or costs in year five were flowed through in the [E]CM". He articulated the rationale for a possible modification as follows:

> Because what -- my thinking is this, and then I'll let you have your reaction to it. My thinking is this: Is that would mitigate the perception that you would postpone costs because of the benefit you would get for five years if you did that. And the other part of my logic is that since the structure of your ECM does not allow you to – it basically provides a disincentive to do a long-term incentive -- make a long-term incentive investment, i.e. to make an investment that's greater than you would get a return on that one year, that there doesn't seem to be a great logic to carry forward benefits from strictly that year through.[167]

104. The Companies submit that the original proposal remains reasonable in light of FortisBC's expressed intention to achieve sustainable savings during the PBR term. That said, the modification to not apply the ECM to net costs or benefits in year 5 is a reasonable one if it would help to assuage concerns. As Mr. Swanson acknowledged at the hearing: "There's some

---

[164] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.47; see also T2:313, l.19-314, l.7 (Roy); T3:400, ll.2-12 (Perttula, Swanson).

[165] T3:400, ll.7-12 (Swanson).

[166] T2:305, ll.17-19 (Roy).

[167] T4:851, l.10-852, l.13 (Swanson). See also T4:740, l.11-742, l.25 (Perttula, Swanson, Roy).

logic to it. It removes that disincentive as you've talked about. It also removes some of the worry that you could play with the numbers at the end, yet it still maintains most of the plan to get you most of the way there in terms of being able to invest in longer term projects that have a longer term payback. So it seems fairly reasonable."[168]

E. SAFEGUARDS - MID-TERM REVIEW AND OFF-RAMPS

105. The majority of PBR plans include provisions that protect customers and the utility against the potential unintended or unexpected outcomes that may occur during the plan's term.[169] These safeguards can vary from provisions that permit modification of a particular element of the PBR design ("re-openers"[170]) to complete regulatory review or termination of the plan ("off-ramps").[171] The Companies propose a Mid-term Review of the PBR Plan (to consider re-openers in appropriate circumstances) and two off-ramps. FortisBC submits that these provisions are appropriate safeguards in the context of the overall PBR Plan.

(a) Mid-term Review

106. The Mid-term Review is a concept that was employed during FEI's 2004 PBR.[172] It will be held as part of the third Annual Review in 2016. The Mid-term Review provides an opportunity for all stakeholders to review the outcomes of the PBR and, if required, to address specific and discrete flaws with an otherwise workable plan.[173] Mr. Swanson elaborated: "The intent is like material unintended outcomes. We don't see it as a means of opening up PBR and tweaking everything. It really is if something's broken, get in there and fix it as opposed to hit an off-ramp and make the plan go away."[174] The PBR Plan should be allowed to play out unless

---

[168] T4:852, ll.20-26 (Swanson).

[169] T4:77, ll.19-26 (Overcast).

[170] Exhibit B2-11, CEC-FEI/FBC IR 3.43.1.

[171] FEI Exhibit B-1, FEI Application, p.76; FBC Exhibit B-1, FBC Application, p.69.

[172] In that case, the review was mainly used as a confirmation that the plan was going well: T4:778, ll.1-11 (Perttula). It is new to FBC: T4:778, ll. 12-15 (Perttula).

[173] T4:781, l.9-782, l.8 (Swanson)

[174] T4:778, l.21-779, l.9 (Swanson); T2:233, ll.6-9 (Swanson); T2:244, ll.8-14 (Swanson); T4:780, ll.10-18 (Swanson).

an element of the PBR Plan is capable of being improved for the mutual benefit of stakeholders.[175]

107. The limited scope of the Mid-term Review is reflected in the proposed terms of reference, which provide for stakeholders to work to identify changes for Commission approval in the event of sustained material changes to service quality, or financial distress. Service quality is addressed in Part 5. The "financial distress" criterion is meant to capture material unanticipated negative outcomes that are outside of the Companies' control and cannot be rectified by an exogenous factor application.[176] FortisBC submits that there is little likelihood of needing to call on either provision at the Mid-term Review, given the balanced PBR Plan and the success of the Companies' prior PBRs.[177]

(b) Off-Ramp Provisions

108. Whereas the Mid-term Review is intended to be a "checkpoint" to permit stakeholders to address specific and discrete flaws with an otherwise workable plan, an off-ramp is a complete regulatory review of the PBR Plan in prescribed circumstances.[178] The two proposed off-ramps are remedies of last-resort for customers or the Companies in the event that the PBR Plan is unable to continue in light of unforeseen circumstances. The Companies submit that the proposed financial and non-financial triggers are appropriate in light of the overall PBR Plan.

---

[175] Exhibit B2-8, BCUC-FEI/FBC IR 3.25.1; Exhibit B2-11, CEC-FEI/FBC IR 3.43.4.

[176] FEI Exhibit B-1, FEI Application, pp.76-77; FBC Exhibit B-1, FBC Application, pp.69-70; Exhibit B2-8, BCUC-FEI/FBC IR 3.24 series; FEI Exhibit B-9, COPE-FEI IR 1.7.8. An example of financial distress might be significant inflationary pressures on sustainment capital expenditures that are not reflected in the province-wide CPI or AWE measures.

[177] Exhibit B2-8, BCUC-FEI/FBC IR 3.24.4.

[178] Exhibit B2-11, CEC-FEI/FBC IR 3.43.5.

Financial Trigger of Off-Ramp

109. Earnings-based off-ramps, which are triggered if the actual ROE of the utility differs significantly from its approved ROE, are the most common form of off-ramp provisions. The Companies are proposing that the PBR Plan be reviewed if the achieved post-earnings sharing ROE of the Company exceeds or drops below the allowed ROE by 200 basis points in any single year of the PBR term (i.e., it is symmetrical). Dr. Overcast considered the inclusion of an automatic quantitative off-ramp provision to be an improvement over the past FEI and FBC PBR plans.[179]

110. Dr. Overcast explained that finding the right balance between maintaining the PBR incentives and safeguarding customers and the Companies is essential when designing earnings-based off-ramps.[180] The trigger point (the variance between earned and approved ROE) should be substantial enough to ensure that the PBR incentive powers are maintained (this is particularly important for a single year trigger point) and at the same time small enough to safeguard against potential excessive profits or losses. The specific threshold proposed as the trigger (+/- 200 bps post-sharing) was a judgment call made by the Companies in consultation with Dr. Overcast. It is higher than the +/- 150 bps threshold used in FEI's 2004 PBR Plan, but accords with the threshold employed in the last FBC PBR plan for recording earnings for future disposition.[181] The Companies submit that their proposed +/- 200 bps trigger achieves the appropriate balance for the following reasons:

---

[179] FEI Exhibit B-1, FEI Application, pp.77-78; FBC Exhibit B-1, FBC Application, pp.70-71.

[180] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada, p.9

[181] Exhibit B2-11, CEC-FEI/FBC IR 3.45.1: The 2004 FEI PBR Plan had a trigger mechanism of 150 basis points (after earnings sharing) above or below the allowed ROE that was not an automatic off-ramp. It was open for parties to request a Commission review of the 2004 FEI PBR Plan if this threshold was exceeded but the 150 basis point threshold was not exceeded in the six-year term. The 2007 FBC PBR Plan had a trigger mechanism of 200 basis points above or below the allowed ROE that was not an "off-ramp". If this earnings threshold was exceeded the earnings variance (positive or negative) would be placed in a deferral account for review and disposition at the next Annual Review.

- The proposed upper bound will only be achieved in the unlikely event that the Companies are able to find very significant savings that could result in excessive profits.[182] If the threshold is set too low, there is a greater risk of triggering the off-ramp prematurely so as to put at risk continued achievement of some of the primary benefits of PBR.[183] FEI came close to the previous ±150 bps threshold at one point in the course of generating benefits for the Company and customers.

- On the bottom bound, 200 basis points is a significant number when the ESM is taken into consideration. Dr. Overcast referred to a 400 basis point reduction in ROE (pre sharing) as being "pretty catastrophic" and indicated "…I'm not aware that any utility would get to the point of being 200 basis points below their allowed return without filing a cost of service application. As a practical matter, you can't allow your business to get that far below the allowed return…".[184]

111. Dr. Overcast summarized the considerations that went into selecting the proposed trigger as follows:

> The off-ramp is designed to give credibility to the plan overall for all stakeholders, and the result is that if you were under cost of service, for example, it would be unusual for a company to wait until they were 200 basis points below their allowed return before they filed to seek a rate increase. And at the same token, it would be unusual if customers weren't complaining if the company was over 200 basis points above their allowed return. So, it gives credibility to the plan to have a range that represents something that would be equivalent to the protection you would have under cost of service for both parties, or for all parties to the proceeding. [185]

FortisBC submits that the proposed financial trigger is indeed appropriate.

---

[182] Exhibit B2-11, CEC-FEI/FBC IR 3.45.5.

[183] Exhibit B2-11, CEC-FEI/FBC IRs 3.45.1, 3.45.3, and 3.45.5.

[184] T4:788, ll.15-19 (Overcast); T4:791, l.22-792, l.10 (Overcast).

[185] T2:255, l.24-256, l.13 (Overcast).

Non-Financial Triggers

112. In addition to the earnings based off-ramp provision, FortisBC has proposed a non-financial trigger of a "sustained serious degradation of the SQIs".[186] This off-ramp provision is the last resort option for dealing with declining service levels, and is similar to the trigger used in FEI's last PBR.[187]

113. Maintaining service quality is an important premise of the PBR Plan, and a sustained degradation of the SQIs is indicative of a more fundamental issue with the PBR Plan. The requirements for service degradation to be "sustained" and "serious" are important.

- First, as described in Part 5 of this PBR Submission, failure to meet one (or more) SQI benchmarks does not necessarily constitute unacceptable performance since by their very nature the benchmarks are averages and under normal circumstances results will be above and below the average. There can also be any number of causes for SQI results to decline, including random one-time events. Triggering of the off-ramp provision would not be warranted in such circumstances.[188]

- Second, there are other, less drastic options available to address declining service levels. At each Annual Review, FEI and FBC will review the SQI results and explain any variances from the benchmarks. If appropriate, the Companies will work cooperatively with interveners and the Commission to address any performance deficiencies. This may prevent the trigger of the off-ramp provision.[189] FortisBC has addressed SQIs in greater detail in Part 5 of this PBR Submission, including addressing Commissioner Cote's comments on SQI performance that falls short of a "sustained serious degradation".

---

[186] FEI Exhibit B-1, FEI Application, p.78; FBC Exhibit B-1, FBC Application, p.71.

[187] T5:1086, ll.13-18 (Swanson).

[188] FEI Exhibit B-1, FEI Application, p.78; FBC Exhibit B-1, FBC Application, p.71; T4:793, l.12-794, l.13 (Swanson).

[189] Exhibit B2-8, BCUC-FEI/FBC IR 3.25.2.

114. Practically speaking, given that the Commission's PBR Decision will be released no earlier than mid-2014, the Mid-term Review will provide the earliest opportunity to assess whether a "sustained serious degradation" is occurring; insufficient time will have passed before then to discern any trend. [190]

F. ANNUAL REVIEW

115. The Companies propose an Annual Review process. It is modelled on the Annual Review process employed in FEI's 2004 PBR Plan and consists of a workshop, one round of IRs from the Commission and Interveners, letters of comment and a Commission determination of rates. The Annual Review process serves two functions:

- ***Updating inputs:*** The Companies will present the current year's projections and the upcoming year's forecasts for a number of items. Flow-through items will be trued-up to actuals for the prior year. Inputs in the formula, such as inflation and customer growth will be re-forecasted. (The prior year's formula-based O&M and formula-based capital expenditures will not be adjusted during the PBR term, other than any limited rebasing for capital outside the +/- 10% threshold in any year).[191]

- ***Transparency:*** The Annual Review is an opportunity for the Commission, interveners and interested parties to review FortisBC's performance during the prior year. The Companies will report on SQI results. The review of the cost of service will not be as detailed as a revenue requirements application would be, since controllable costs are largely formula driven; nevertheless, the Annual Review will provide more frequent reporting than would normally exist under COS regulation.[192]

---

[190] Exhibit B2-8, BCUC-FEI/FBC IR 3.25.1.

[191] Exhibit B2-11, CEC-FEI/FBC IR 3.48.1; T2:244, l.15-245, l.4 (Swanson).

[192] T2: 243, l.17-244, l.7 (Swanson).

116. Based on past experience under FEI's 2004 PBR Plan, there is every reason to expect that the Annual Review process is an appropriate mechanism for addressing these objectives.[193]

[193] FEI Exhibit B-1, FEI Application, pp.78-79; FBC Exhibit B-1, FBC Application, pp.71-72; Exhibit B2-11, CEC-FEI/FBC IR 3.47.2; T6:1201, l.19-1203, l.2 (Loski).

PART FOUR: THE (I-X) FORMULA

117. Part Four of this PBR Submission addresses the I-X formula, which was a significant focus in the proceeding. The Inflation Factor (or "I-Factor") is a forward looking measure of the inflation pressures that the Companies must manage each year of the PBR period. The X-Factor, also known as the productivity improvement factor, represents the amount by which the utility is expected to outperform the industry and economy-wide productivity gains. The X-Factor serves as a forward-looking benefit sharing mechanism under PBR whereby the utility allocates the expected X-Factor productivity gains to customers, regardless of the firm's realized productivity.[194] In this case, the Commission should find:

- First, the Companies have proposed a logical and reasonable basis for determining the I-Factor, which can be expected to reflect cost pressures they will face during the PBR period.

- Second, a fixed X-Factor of 0.5% exceeds Dr. Overcast's measured industry and economy wide productivity levels by a significant margin, and presents a challenge to the Companies to seek additional efficiencies.

- Third, the reasonableness of FortisBC's proposed X-Factor is supported by:

    - the accelerated infrastructure replacement being undertaken in the gas and electric utility industries, which mathematically drives a negative Total Factor Productivity ("TFP");

    - the recent findings of Dr. Lowry's company, Pacific Economics Group ("PEG"), in an Ontario Energy Board ("OEB") proceeding of a negative TFP for the Ontario electric utility industry;

[194] FEI Exhibit B-1, FEI Application, per Dr. Overcast, p.48.

- the fact that the proposed X-Factor of 0.5% results in a rate trajectory for FEI and FBC that is lower than what is yielded by the forecasts included in the Applications; and

- the fact that Drs. Overcast and Lowry incorporate stretch factors within their recommended X-Factors that are smaller than the stretch factor implicit in the 0.5% X-Factor proposed by FortisBC.

- Fourth, Dr. Lowry's recommended X-Factors are overstated by virtue of upward biases inherent in aspects of his TFP methodology, and the fact that material assumptions in his TFP analysis are unrealistic for utilities.

A. PROPOSED INFLATION FACTOR (I-FACTOR) IS REASONABLE

118. The Inflation Factor (or I-Factor) recognizes that utility costs are subject to the general inflationary pressures occurring in the economy, although the specific pressures or weightings of the various inflationary influences on the Companies' costs may be different than for the economy in general. The Companies' previous PBR plans calculated an average inflation rate for British Columbia using a combination of sources for CPI forecasts ("BC-CPI"). FortisBC is proposing to employ a weighted composite I-Factor, with labour indexed to BC Average Weekly Earnings ("BC-AWE")[195] and non-labour costs continuing to be indexed to BC-CPI.[196] The Commission should find, for the reasons set out below, that the composite labour and non-labour inflation index:

- is a reasonable means of determining the I-Factor that is more reflective of FortisBC's labour and non-labour costs than using BC-CPI alone;[197]

- is weighted appropriately to reflect FortisBC's labour and non-labour mix;

---

[195] BC-AWE has been renamed to Average Weekly Wages & Salaries Per Employee ($, Industrial Composite): Exhibit B2-2, CEC-FEI IR 3a.22.2.

[196] FEI Exhibit B-1, FEI Application, p.46; FBC Exhibit B-1, FBC Application, p.42.

[197] FEI Exhibit B-1, FEI Application, p.46; FBC Exhibit B-1, FBC Application, p.42.

- should be based on forecasts for the coming year, not "trued-up" inflation for the year; and

- should be preferred to GDPIPIFDD (the index proposed by Dr. Lowry).

(a) Composite I-Factor More Reflective of FortisBC's Costs than BC-CPI Alone

119. FortisBC's proposal to incorporate a labour-based index into the I-Factor is a straightforward and transparent means of making the I-Factor more reflective of the Companies' labour and non-labour costs than it was in the Companies' previous PBR plans.

120. BC-CPI is an economy-wide inflation measure. Labour is subject to different inflationary pressures than the economy as a whole. BC-AWE is published by a reputable, independent agency and is published on at least an annual basis. It is also reasonably stable.[198] BC-AWE only measures changes in labour, and does not incorporate changes in pensions (Dr. Lowry incorrectly stated in BCUC IR 2.20.1 that BC-AWE includes pension and benefits). The pension exclusion lends support to using BC-AWE, since it is applied to FortisBC's costs that exclude pensions.

121. Dr. Overcast endorsed the change to incorporate a BC-AWE, indicating in his report that a composite index "is a better reflection of price changes."[199] He added at the hearing:

> Well, I frankly think that the way this I factor has been put together in two pieces, one piece to represent direct labour and another piece that represents general inflation, is a reasonable method. And I think that the key point is that you want an index that will give you some confidence that it's going to be appropriate index for the costs that have been going up for the companies. And

---

[198] FEI Exhibit B-1, FEI Application, p.46; FBC Exhibit B-1, FBC Application, p.42. BC-AWE forecasts, as with BC-CPI, are published by the federal and provincial governments, as well as by three of Canada's largest financial institutions.

[199] FEI Exhibit B-1, FEI Application, p.46; FBC Exhibit B-1, FBC Application, p.42; Dr. Overcast discussed the precedent and rationale for the use of the weighted composite I-factor in FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada at pp.35 and 46.

> the fact that you've used CPI in the past and it's been successful seems to me to be a basis for keeping that for the non-labour component.[200]

122. A weighted composite I-factor that incorporates a labour-specific index has now been adopted by the AUC and the OEB.[201]

(b) Weightings Selected Reflect FortisBC's Mix of Labour and Non-Labour

123. The composite factor weightings should, and do, reflect FortisBC's proportion of labour and non-labour costs. The 45% non-labour/55% labour split was based on analysis of the Companies' recent and forecast costs. [202]

124. FortisBC was asked about whether there is double counting of labour in using a composite index because BC-CPI (which is to be used for the 45% non-labour costs) also includes a labour component. Dr. Overcast explained that "it's appropriate that there be a labour component in it because there's a labour component in all for the things that you buy under the operating expense or capital as well", and it is a cost of producing the product.[203] Mr. Swanson provided an illustration:

> …if we take as an example the cost of a transformer that we purchase, the transformer includes the labour that the transformer manufacturer used to assemble or build the transformer. So, that non-labour component of acquiring the transformer does include a labour cost. So, if the CPI does, so does the actual cost of the component we purchase.
>
> Now, we also still incur the labour costs that when we go to hang that transformer. So, the fact that the transformer had labour imbedded in it, and the fact we incur labour when we go hang that transformer is consistent with the

---

[200] T2:318, ll.15-25 (Overcast).

[201] FEI Exhibit B-1, FEI Application, p.47. Ms. Roy explained that FortisBC identified the need to incorporate a labour-specific index after determining in the last FEI RRA that CPI was not, on its own, representative of FEI's costs. The Companies then became aware of the developments in other jurisdictions: T2:288, ll.4-20 (Roy).

[202] FEI Exhibit B-1, FEI Application, p.47; FBC Exhibit B-1, FBC Application, p.43.

[203] T2:319, ll.3-12 (Overcast). FortisBC provided responses to IRs that quantified the amount of labour that go into non-labour component of the Companies' costs: FEI Exhibit B-6, BCPSO-FEI IR 1.13.2; Exhibit B2-11, CEC-FEI/FBC IR 3.12.4; T2:319, ll.13-23 (Roy).

> fact that the CPI has labour in it, and you are using an average weekly earnings for the labour component. We don't actually think there is a double count.[204]

125. The above logic does not change based on whether goods are manufactured in BC; BC-CPI reflects the price of goods and services purchased by consumers in BC, not manufactured in BC.[205]

(c) Use of Forecast Inflation for Following Year is Appropriate.

126. FortisBC is proposing to update the inflation forecasts at each Annual Review to adjust the formula for the upcoming year's rate determination.[206] There are two reasons why the I-Factor should be based on forecasts for the coming year, not "trued-up" inflation for the year.

127. First, FortisBC submits that using forecast inflation as the input in a formula is conceptually more appropriate than "truing-up" BC forecasts to BC actual because the forecast more closely reflects the cost pressures experienced by the Companies.[207] Ms. Roy and Mr. Swanson explained that this is the case for both labour (BC-AWE) and non-labour (BC-CPI) components of costs. For instance:

- Labour costs are influenced by collective agreements that are based on forecasts. Once a collective agreement is in place, the fact that BC-AWE comes in higher or lower than the forecast inflation is moot. FEI's next labour agreement has yet to be negotiated, and the electric agreement is subject to arbitration.[208]

---

[204] T3:580, l.15-581, l.9 (Swanson).

[205] Mr. Miller asked Mr. Swanson about whether the location of production matters. Mr. Swanson incorrectly agreed that it was a theoretical problem without realizing that BC-CPI is based on the location of goods and services purchased. CPI is, as its name suggests, a consumer price index that reflects prices paid by consumers.

[206] FEI Exhibit B-1, FEI Application, p.48; FBC Exhibit B-1, FBC Application, p.44. The weighting would remain constant: T3:597, ll11-22 (Roy) regarding Exhibit A2-23.

[207] T2:283, ll.7-15 (Roy).

[208] T3:588, l.12-592, l.11 (Swanson, Roy).

- The Companies purchase a lot of materials under contract with long lead times. FortisBC will evaluate the price offered by a supplier based on forecast inflation:

> …we're going to look at what inflationary -- what inflation levels are expected and to see if those contract prices, see if those increases in the contract are in the ballpark of the expected inflation…
>
> The fact that actual CPI may have come in, like in 2009 at zero, is somewhat irrelevant because you've already placed your orders or you've already entered into your contracts, and your costs aren't going to be driven by zero. They're going to be driven by the orders in the contracts that you've placed.[209]

- Over half of the non-labour cost is contractor costs, and most of those contracts are negotiated in advance.[210]

128. The fact that utility costs influenced by forecast inflation in the above manner "tend not to change (or change much) if actual inflation is higher or lower than forecast"[211] differentiates inflation from flow-through items that are "trued-up" at the Annual Review.[212] Ms. Roy observed that "in our cost of service applications, even, and our own internal budgeting, we use forecasts of inflation to determine those amounts…".[213]

129. Second, historic comparisons suggest that there is little practical difference between forecast and actual and the variances will be both positive or negative. Although the average actual BC-CPI for the past ten years was slightly lower than forecast, the variance was almost entirely due to one year - 2009 - when actual inflation dipped to zero. If that anomaly is removed, the forecasts essentially track actual on average for the other nine years.[214] Future

---

[209] T3:586, l.18-587, l.14 (Swanson); T2: 282, ll.7-20 (Roy).

[210] T3:587, ll.15-25 (Roy).

[211] Exhibit B2-8, BCUC-FEI/FBC IR 3.6.3; T3:582, l.7-583, l.17 (Roy).

[212] T3:584, l.18-587, l.25 (Roy, Swanson).

[213] T2: 282, ll.7-20 (Roy). See also: T3:584, l.18 -586, l.12 (Roy, Swanson).

[214] T2:281, ll.11-23 (Roy); Exhibit B2-11, CEC-FEI/FBC IR 3.15.2, revised in FEI Exhibit B-1-5, Attachment 3. Commission Staff presented a witness aid (Exhibit A2-23) that appeared to suggest that, in past years, actual BC

anomalies, if any, could be either higher or lower. Given how close forecasts have tracked to actuals overall, there is little practical reason to consider departing from the established practice of using forecasts.

130. FortisBC's proposal is conceptually appropriate, fair to all parties, and efficient.

(d) Dr. Lowry's Proposal to Use BC-GDPIPIFDD

131. Dr. Lowry has proposed using an index referred to as BC-GDPIPIFDD to represent the I-Factor instead of BC-CPI. BC-GDPIPIFDD less familiar to most, if not all, stakeholders than BC-CPI. Although Dr. Lowry states several times that BC-CPI has historically been higher than BC-GDPIPIFDD, his own historical comparison of BC-GDPIPIFDD to BC-CPI (Exhibit C1-0-1) shows that over the 10 years 2003-2012 BC-CPI was 1.65% whereas BC-GDPIPIFDD was 1.76%. BC-GDPIPIFDD was actually *higher*. There is no compelling reason to adopt an unfamiliar and potentially less-transparent index when FortisBC's proposed composite index yields reasonable results.

B. FORTISBC'S PROPOSED X-FACTOR IS APPROPRIATE

132. This section explains why FortisBC's proposed 0.5% X-Factor is reasonable. We make two main points:

- First, FortisBC's proposed X-Factor of 0.5% accounted for Dr. Overcast's expert recommendation of a zero X-Factor, which in turn was based on the results of measured industry productivity (TFP) and reasonable upward adjustments including a stretch factor.

---

inflation has generally come in below forecast BC inflation. Ms. Roy identified several errors in the witness aid that resulted in the past variances being significantly overstated. Very different results could be obtained simply by changing Staff's choice of time period. After canvassing the issues with the witness aid, Ms. Roy concluded: "So it's an interesting illustration but I don't know if it actually tells us anything about what would actually happen to customers based on this." T3:596, l.23-598, l.7 (Roy).

- Second, management's decision to propose a higher X-Factor of 0.5% provides greater immediate benefits to customers and presents a significant productivity challenge.

(a) The Basis for Dr. Overcast's Recommended Zero X-Factor

133. Dr. Overcast recommended a zero X-Factor for both FEI and FBC. The zero X-Factor was the sum of three components, which are discussed below: (1) the negative TFP that he measured for the gas and electric industries; (2) an upward adjustment to account for the fact that the TFP calculations for companies in the sample included some flow-through costs (e.g., pension) and all capital, whereas FortisBC (the utilities to which the TFP results are being applied) is proposing to exclude CPCN capital and some flow-through costs from the formula;[215] and (3) an upward adjustment, referred to as a "stretch factor", that Dr. Overcast determined based on his experience and FortisBC's past history with PBR. Dr. Overcast's approach was reasonable, and his X-Factor recommendation was sound, for the reasons described below.

Dr. Overcast's Approach to Measuring TFP for Gas and Electric Industries

134. TFP is "a measure of how efficiently a firm converts total inputs into total outputs", expressed by the formula TFP = change in outputs - change in inputs.[216] Dr. Overcast described his approach to calculating TFP for the gas and electric industries in two reports filed with the Applications.[217] In essence, Dr. Overcast used his understanding of utility business economics and operations to design a reasonable TFP methodology that addressed shortcomings with applying the traditional TFP model to regulated gas and electric utility industries that do not fit the academic paradigm.

135. Dr. Overcast's methodology for determining TFP for the electric and gas industries involved four main steps: (1) identifying a broad sample of gas and electric utilities to

---

[215] T3:465, l.19-466, l.12 (Overcast).

[216] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.1.

[217] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4); FBC Exhibit B-1-1, FBC Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-8).

represent the electric and gas utility industries; (2) compiling actual cost and operational data for each utility for each year of the sample period to determine actual physical inputs and outputs; (3) calculating TFP (i.e., change in outputs minus change in inputs) for each utility in the sample, for each year of the study; and (4) using the calculated TFP for each company in the sample to arrive at a central tendency for each industry.

136. The key parameters of Dr. Overcast's gas and electric TFP studies, and Dr. Overcast's rationale for using those parameters, were as follows:

- ***Choice of sample companies:*** Dr. Overcast compiled TFP data on large samples of U.S. gas and electric utilities.[218] The purpose of looking at a broad sample of utilities, rather than looking at FortisBC's operations specifically is "to get some measure of the central tendency of productivity as opposed to what's happening in a given utility."[219] He used U.S. utilities because there is a centralized database of U.S. utility data, which does not exist in Canada. U.S. data can be used because of the similarities in operating conditions across North America.[220] U.S. data has been used in other Canadian jurisdictions, and Dr. Lowry used it in this case as well.[221]

- ***Measurement period:*** Dr. Overcast's study used a five-year measurement period (2007-2011). He considered this period to be most representative of the business conditions expected to be faced by the gas and electric industries

[218] 95 US-based natural gas LDCs operating in 30 states: FEI Exhibit B-1, FEI Application, p.52. 72 US-based electric utilities: FBC Exhibit B-1, FBC Application, p.48.

[219] T2:224, l.25-225, l.2 (Overcast).

[220] T2:224, ll.14-20 (Overcast). See also: FEI Exhibit B-1, FEI Application, p.52; FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.8. FBC Exhibit B-1, FBC Application, p.48; FBC Exhibit B-1-1, FBC Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-8), p.8.

[221] Drs. Overcast and Lowry both used broad samples of U.S. utilities due to limitations in Canadian data. Their respective samples overlap significantly. Both experts have included utilities of a broad range of sizes, in various regions, with varied operating histories. FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.8. T7:1349, l.16-1350, l.13 (Lowry).

during the PBR term.[222] As will be discussed later in this Part, gas and electric utilities across North American have embarked on huge infrastructure replacement programs. Accelerated investment in system modernization requires significant increases in inputs without generating corresponding increases in outputs. As a result, utilities across North America are experiencing negative TFPs (zero change in output minus a positive input value equals a negative number) to an extent not seen in the years prior to Dr. Overcast's sample period. The effect of the recession on TFP during the study period is dwarfed by this phenomenon.

- ***Output Measures:*** Outputs (the first of two variables in the TFP formula) are the physical outputs generated by a firm. The outputs of a utility delivery system reflect the physical ability to deliver, as opposed to the commodity itself.[223] An output measure must reflect what is driving utility costs.[224] Dr. Overcast's analysis for FEI is based on three different output measures: customers served and system capacity, and a density-weighted composite factor of these two variables.[225] For FBC, there are four output measures: two different weighted capacity and customer measures, as well as customers and capacity separately.[226] These output measures reflect widely accepted cost drivers employed in utility Cost of Service Allocation ("COSA") studies.

- ***Input Measures:*** Inputs (the other variable in the TFP formula) are the physical inputs that are used in producing outputs. Dr. Overcast's input measure included a capital component and a composite component that reflected labour, materials, services, and rents. He measured the capital component as Operating

[222] FEI Exhibit B-1, FEI Application, p.52; FBC Exhibit B-1, FBC Application, p.48.

[223] By analogy, a courier company like Fedex produces a delivery system for parcels. It does not produce the parcels themselves: T7:1445, l.13-1446, l.10 (Lowry).

[224] T7:1445, ll.2-12 (Lowry).

[225] FEI Exhibit B-1, FEI Application), p.52.

[226] FBC Exhibit B-1, FBC Application, p.48.

Revenue excluding gas costs and all other O&M expenses. The resulting revenue represented the cost of capital including return, depreciation, and taxes. The measure of all other costs was a direct composite measure as reported in the financial reports of each company in the sample.[227] Dr. Overcast used in his calculations actual *ex post* data for each utility, for each year. He elaborated as follows:

> The input measure is developed from a capital component and a composite component that reflects labor, materials, services, and rents. Both inputs are measured on an ex-post basis using actual financial data for each natural gas LDC. The ex-post cost of capital is measured as Operating Revenue excluding gas costs and all other operating and maintenance expenses. The resulting revenue represents the cost of capital including return, depreciation, and taxes. The calculation of this cost is based on a method that the Federal Energy Regulatory Commission (FERC) refers to as the Kahn Method based on its use in setting the price cap index for oil pipelines regulated by the FERC. The method was developed by Alfred Kahn, a noted regulatory economist, in his initial expert testimony presented in a 1993 regulatory proceeding related to the regulation of oil pipelines under price cap regulation. It is useful to note that the Federal Communications Commission also used the method in telecommunications and that the method has been discussed in reports to the Australian Energy Regulator. The measure of all other costs is a direct composite measure as reported in the financial reports of each company. This method benefits from not having to develop a composite measure or to estimate the quantity of each input used from data that does not permit direct measurement of the quantity of the factor used.[228]

137. Dr. Overcast explained that a key impetus for taking the approach he did was that he recognized, based on his practical experience and recent productivity literature, that there are problems with applying the traditional TFP model to the actual conditions faced by regulated utilities:

---

[227] FEI Exhibit B-1, FEI Application, p.52; FBC Exhibit B-1, FBC Application, p.48.

[228] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.10.

> When we undertook this assignment, we knew that there were shortcomings associated with the academic model for calculating TFP and ultimately the X factor. We knew that, because I keep up with the literature on things related to regulation, and since 1996, if you read the economics literature, the literature talks about a lot of significant changes that have occurred….
>
> Now, based on those factors, and the fact that I have a practical understanding of how the industry operates, and I also have a practical understanding of the data that's used to calculate a TFP study, there was no reason that we should not prepare a TFP analysis that would be reflective of the realities of the gas and electric business as opposed to this purely theoretical model.[229]

138. One of the key characteristics of the academic TFP model is to assume a high degree of uniformity among companies within an industry when it comes to technology mix, labour mix, materials, plant, equipment and cost of capital. This competitive market assumption manifests itself, for instance, in the use of cost indexes in input calculations (as Dr. Lowry's study uses), which implicitly requires assuming that all sampled companies use the same mix of inputs and experience the uniform cost pressures that are reflected in the index. While the assumption of uniformity makes sense in the context of a competitive industry, it does not make sense in the context of regulated utilities for the very reasons that cause utilities to be regulated in the first place - sunk costs and lumpy investments.[230] An index cannot reflect the actual mix of inputs used by individual utilities to the extent that it would in competitive industries.

139. In the context of a TFP study, even small instances of measurement error associated with ill-fitting assumptions can add up to very significant errors in the resulting TFP. As discussed later, we see this compounding effect in Dr. Lowry's study based on the way that he determined inputs. The key point is that Dr. Overcast's approach of directly measuring inputs for each utility using hard *ex post* data avoided the need to measure inputs indirectly using cost indexes to represent aggregated data for the industry. Dr. Overcast elaborated:

---

[229] T3:457, l.13-458, l.6 (Overcast).

[230] Exhibit B-45, Overcast Rebuttal Evidence, p.38.

> The idea [under the traditional approach] is that essentially if you take the equation that price times quantity equals total cost, and you solve for quantity [i.e., inputs] divided by -- dividing total cost by price, the idea there is that if a utility has higher price for labour because they're in a higher-cost labour market, when you divide that number into their total cost, you're going to get a lower number of physical input units. And the same thing would be true if they had a lower price. You'd get more physical input units.
>
> So the mix of labour impacts the way you calculate the inputs, and since the price indexes aren't set up -- a typical price index isn't set up in a way to take into account all the local issues. In fact, if you look at the Handy Whitman index, they say that's -- they say that is a caution in using their index. That it -- you need to test it against the local conditions.
>
> And so, recognizing that as a problem, you have to find some reasonable solution for measuring inputs and we chose to use a measure based on the Khan method that's been accepted at the FERC. And while it's not -- while it is not as elegant and mathematically complex as the traditional academic model, the whole point is you want to get something that gives you a reasonable estimate that people can understand, it is transparent, and it is at a level that sort of consumable by the people who have to understand it.[231]

Dr. Overcast's approach, in addition to recognizing the uniqueness of each utility, was transparent because "the estimates are based on actual data that is available from public sources and the calculation of the composite factors are straight forward…".[232]

[231] T3:571, l.20-572, l.23 (Overcast).

[232] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.10; Exhibit B-45, Overcast Rebuttal Evidence, p.4.

Understanding Dr. Overcast's Measured Negative TFP for Electric and Gas Industries

140. Dr. Overcast's two TFP studies yielded the following negative TFP values for the electric and gas industries:

	Gas Industry[233]	Electric Industry[234]
Average	-4.1%	-4.9%
Range	-3.2% to -4.9%	-3.9% to -5.5%

Understanding what causes a negative TFP value, and its significance, is fundamental to understanding why Dr. Overcast's measured negative TFP values make more sense than Dr. Lowry's large positive values in the present circumstances.

141. Given the nature of the TFP formula (*TFP = change in outputs - change in inputs)*, TFP will be negative as a matter of mathematics when the *change in outputs* is less than the *change in inputs*. It will be positive when the reverse is true. The negative values that Dr. Overcast measured for the electric and gas industries are attributable to the utilities in Dr. Overcast's large samples tending to experience a significant increase in physical inputs (measured based on hard, *ex post* data for each utility for each year) that exceeded the change in outputs as measured by customers and capacity. This will occur, for instance when utility infrastructure is being replaced:

> Well, the negative TFP occurs because in this instance there's a lot of infrastructure replacement going on, and the idea behind TFP is to measure the change in outputs minus the change in inputs. And obviously if you're replacing pipe in the ground or wires overhead, with no growth, no change in output, then your costs are rising faster and your inputs, you're using more inputs than you are outputs and so you would have a negative TFP factor.[235]

[233] TFP numbers were revised in FEI Exhibit B-1-4, Errata, December 13, 2013.

[234] TFP numbers were revised in FBC Exhibit B-1-8, Errata, December 13, 2013.

[235] T2:227, ll.2-10 (Overcast).

In practice, a negative value means that sampled utilities' rates are rising faster than inflation.[236]

142. It is important not to confuse the TFP sign (+/-) with an assessment of efficiency. A negative TFP is not synonymous with being inefficient, and a positive TFP is not synonymous with being efficient.[237] Drs. Overcast and Lowry agree that a company can be efficient with a negative TFP and an inefficient company can have a positive TFP.[238] Dr. Overcast gave some practical examples at the hearing to demonstrate why it would be a mistake to equate high cost (input) operations or a negative TFP with inefficiency, and *vice versa*:

> Con Edison, which serves New York City, except in an emergency they can't cut a street to make a repair during the day. They can only do it in overnight hours. Okay? So that means that all their normal maintenance work has to be done in the middle of the night. That's, you know, there's some other complications with doing that. So they tend to be one of the highest cost O&M customer of any utility, and if you just said, "Well, I've benchmarked their O&M cost and this is a much higher number, therefore they're inefficient," you'd be dead wrong.
>
> They may be very efficient, given the circumstances that they have to operate under. And you can just -- and you can go through and find a lot of different things that impact that. And so, unless you can control for all those variables, it's very difficult to say that one utility is more efficient than another, just based on the things you can observe like an output point and the inputs used to produce that point.[239]

143. We discuss later in this Part how Dr. Overcast's measured negative TFP for the gas and electric industries is explained by accelerated industry-wide investment in infrastructure replacement that does not add new customers or capacity (outputs).

---

[236] T2:226, ll.21-25 (Overcast).

[237] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.2; T2:227, ll.16-19 (Overcast); T3:385, l.21-389, l.21 (Overcast); T3:409, l.1-410, l.16 (Overcast).

[238] T7:1351, l.24- 1354, l.4 (Lowry).

[239] T3:388, l.2-392, l.17 (Overcast).

Upward Adjustment of Measured TFP

144. Dr. Overcast recognized that the X-Factor must reflect an upward adjustment to the measured TFP values to account for the terms of the Companies' proposed PBR Plan.[240] He explained:

> B&V and FEI are in agreement that B&V's TFP Report produces a more negative TFP number than would be applicable to FEI by virtue of how TFP data has been provided for the sample companies in TFP Report. The capital component in B&V's study is measured as the difference between operating revenue (excluding gas costs) and all other O&M expenditures, and which therefore includes all capital costs, whether pertaining to base capital or growth spending, as well as the infrastructure replacement programs that have been more prevalent in recent years. In contrast, in FEI's proposed PBR Plan, large capital projects approved as CPCNs are excluded from the (I-X) mechanism and are treated under a separate regulatory approval process. Due to limitations in the data used in the TFP Study, the revenue earned by the surveyed companies from these types of infrastructure projects or other particular categories of capital cannot be separated from the capital component as a whole. Therefore, a certain degree of educated judgement is required to adjust the TFP value for the companies in the study. The effect of FEI's proposal to exclude CPCN type projects from capital expenditures subject to the I-X mechanism is to moderate the measured negative TFP value applicable to the industry as a whole.[241]

145. Dr. Overcast indicated (and, as discussed later, Dr. Lowry agreed) that there is no recognized way of quantifying an adjustment; an analysis would require the impractical task of parsing each sampled utility's financial data over many years. As such, Dr. Overcast employed his professional judgment. He concluded that, with the necessary adjustment (and before applying a stretch factor), the X-Factor is still "probably a small negative".[242]

146. Dr. Overcast elaborated on how he formed his judgment as to the appropriate adjustment in response to questions from Commission Counsel:

---

[240] FEI Exhibit B-1, FEI Application, pp.52-53; FBC Exhibit B-1, FBC Application, pp.48-49.

[241] FEI Exhibit B-1, FEI Application, pp.52-53. FBC Exhibit B-1, FBC Application, pp.48-49 with respect to FBC. See also: T2:361, ll.14-25 (Overcast); T3:466, l.14-467, l.10 (Overcast); T3:507, ll.5-17 (Overcast).

[242] T3:508, ll.4-24 (Overcast); T3:569, l.17-571, l.2 (Overcast). PEG in Ontario took essentially the same approach as Dr. Overcast.

> So, I mean, it's part of the art of this, instead of science. There is no scientific way to get to the right number. And you just have to use judgment, and, you know, your judgment is based on your cumulative experience. And I've been doing this work for gas and electric utilities for nearly 40 years. I have a pretty good understanding of how they operate. I mean, I'm not an engineer, but I understand that. I'm not an accountant, but I understand that. And so, I used my judgment and said, you know, this TFP is not representative of the plan [t]hat's being proposed here, and you've got to make some adjustments, and I made those adjustments based on my judgment, which is as a result of a lot of experience actually working for these utilities, gas and electric.[243]

Dr. Overcast has demonstrated a solid understanding of the utility industry generally, as well as the operations of specific utilities in his sample. The Commission should conclude that Dr. Overcast's recommended X-Factor of zero properly accounts for the necessary upward adjustment, as well as a reasonable stretch factor (discussed next).

Incorporation of a Stretch Factor

147. A stretch factor is an upward adjustment from the measured and adjusted TFP that confers additional benefits on customers irrespective of how the utilities ultimately perform under the PBR Plan. Or, as Dr. Overcast, put it: "…you're saying that we're going to hold the utility to a standard higher than the average expected change in total factor productivity for the industry."[244] A stretch factor is implicit in Dr. Overcast's recommended zero X-Factor, and its size reflects the fact that FEI and FBC have already been in PBR for a number of years. Dr. Overcast explained that "stretch factors generally decline as you have more and more experience under PBR, because you've taken advantage of the easiest savings that you can make."[245] This is intuitively correct - it is an illustration of the law of diminishing returns. Dr. Lowry employed similar logic to arrive at an explicit stretch factor of 0.2%, based on an assumption that the Companies operate at average efficiency.[246] He noted that FortisBC

---

[243] T4:625, l.12-626, l.1 (Overcast).

[244] T3:448, l.23-449, l.1 (Overcast). Mr. Swanson added: "[I]t's embedded in the formula when setting rates right at the onset, customers will start receiving benefits immediately in terms of their rate for 2014 currently reflects that reality of that. That productivity factor will be embedded." T3:445, l.25-446, l.5 (Swanson).

[245] T3:449, ll.9-13 (Overcast).

[246] T7:1489, l.15-1491, l.8 (Lowry).

is "not known to be inefficient, that I know."[247] The magnitude of the benefits from the Companies' last PBR plans demonstrates that very significant efficiencies have already been extracted; those savings are no longer available to the Companies.

148. Although FEI and FBC have been out of PBR for some time (4 years for FEI and 2 years for FBC), it would be unreasonable to assume that the savings achieved during PBR have not been sustained. The Commission rebased the Companies' costs and vetted their respective revenue requirements coming out of PBR during intensive hearing processes. In order for the Commission to now find that the savings haven't been sustained, it would have to revisit the findings of the past Commission decisions. There are no grounds to do so. The Commission should operate on the basis that the last PBRs generated sustained savings that continue to be reflected in the base year costs.

(b) Management Decision to Increase the X-Factor to 0.5%

149. Dr. Overcast's opinion is that, accounting for the measured TFP and the appropriate upward adjustment and stretch factor, "the X-Factor should be no higher than approximately zero in order to be theoretically justifiable within the context of FEI's PBR Plan."[248] FortisBC made a management decision to increase the stretch factor to yield the proposed X-Factor of 0.5%. Mr. Swanson explained that the Companies were concerned that "people are going to interpret that [i.e., a zero X-Factor] as you're not embedding any productivity", even though zero would include a stretch factor already. The much larger stretch factor was intended to demonstrate the Companies' commitment to provide an immediate and material benefit to customers under PBR, and in turn improve the prospects of implementing a successful PBR.[249] FortisBC arrived at 0.5% after considering Dr. Overcast's recommended zero X-Factor, and noting that the higher X-Factor in Alberta (1.16%) was being applied to utilities

[247] T7:1492, ll.5-19 (Lowry).

[248] FEI Exhibit B-1, FEI Application, p.53; FBC Exhibit B-1, FBC Application, p.49.

[249] T3:448, l.16-449, l.13 (Overcast); T3:450, l.11-454, l.15 (Overcast, Swanson).

that had never been under PBR and so would logically overstate the X-Factor for utilities with a long history under PBR.[250]

150. Mr. Swanson assessed the proposed X-Factor of 0.5% to be a stretch "…in terms of with a reasonable level of additional effort and some success in that effort that we could achieve it, yes."[251] This is the proper way to look at an X-Factor. An X-Factor must be reasonably attainable, accounting for payback over the PBR term, in order to meet the just and reasonable standard. The ESM is included in the PBR Plan to address the potential for the Companies to achieve savings in excess of the efficiencies inherent in the formula.

C. OTHER CONSIDERATIONS SUPPORTING PROPOSED X-FACTOR

151. There are several factors that, in addition to the negative measured TFP value in Dr. Overcast's TFP studies, support the reasonableness of FortisBC's proposed X-Factor of 0.5%. They are:

- First, the negative measured TFPs being experienced in recent years coincide with the acceleration of large-scale infrastructure replacement in the gas and electric industries;
- Second, Dr. Lowry's colleagues at PEG are now measuring a negative TFP for the Ontario electric industry;
- Third, the FEI and FBC rates arising from the proposed I-X formula will lead to average revenues for the Companies that are lower than the revenues that would be yielded by the average rates based on the forecasts included in the Applications; and

[250] T3:509, l.17-510, l.10 (Swanson); T3:519, l.21-520, l.7 (Roy).
[251] T3:447, ll.8-10 (Swanson).

- Fourth, Drs. Overcast and Lowry agree that the proposed X-Factor should reflect FortisBC's long history of PBR, and both recommend stretch factors smaller than the stretch factor incorporated in FortisBC's X-Factor proposal of 0.5%.

(a) Industry-Wide Infrastructure Replacement Driving Negative TFP

152. Dr. Overcast explained that "the downward trend of TFP growth is mainly caused by capital intensive infrastructure replacement programs in both natural gas and electric utilities, which drive up input costs without increasing output."[252] He "expects that this trend will continue during FEI's proposed five year PBR term."[253] The evidence discussed below demonstrates:

- First, as a matter of mathematics, accelerating infrastructure replacement or other capital investments that do not add customers or capacity drive a negative TFP; and

- Second, such investments are currently occurring in the gas and electric industries and will continue during the PBR term.

Understanding How Infrastructure Investment Drives Negative TFP

153. The replacement of utility infrastructure or other capital investments that does not increase the customers or capacity served will drive negative TFP for utilities because (a) capital is of primary importance in a utility's production function, and (b) the capital investment adds inputs without a corresponding increase in outputs.

154. TFP equals change in *total* outputs minus change in *total* inputs, and thus reflects all elements of a utility's production function. The individual elements of the production function include labour and capital. Dr. Overcast indicated that labour productivity has historically increased and will continue to increase in the future (in part moderated by the

[252] FEI Exhibit B-1, FEI Application, p.51; FBC Exhibit B-1, FBC Application, p.47.

[253] FEI Exhibit B-1, FEI Application, p.51. FBC Exhibit B-1, FBC Application, p.47 in the case of FBC.

increasing wages paid to labour). Since labour generates more outputs for unit of inputs than it did in the past, labour is having an upward influence on TFP. However, the capital component of a utility's production function exerts a much larger influence on TFP than labour because of the capital intensity of utility service.[254] At present, capital is exerting a significant downward influence on TFP that more than offsets the favourable impact of improved labour productivity.

155. Dr. Overcast explained in his TFP Report for Gas that "the economics of infrastructure replacement, all else equal, requires a rate trajectory greater than the rate of inflation just based on the revenue requirements associated with a growth in rate base without any offsetting growth in revenues absent the rate increase required to support the new plant." In the context of TFP, adding physical inputs of pipes, valves, regulators etc. that do not increase outputs for the system mathematically has a downward influence on TFP. If sufficient replacement activity is being undertaken, it will yield a negative TFP for the utility.[255] Dr. Overcast expanded in his Evidence:

> The negative productivity for capital is explained by the need to replace aging infrastructure. In terms of capital costs, an aging infrastructure has been almost fully depreciated. Further, because of the age of the asset and the higher capital costs for replacement due to inflation in both labor and capital, the replacement costs will be even greater than the original cost of the asset replaced. The total capital costs of the utility will increase due to replacing aging infrastructure. By definition, the infrastructure replacement does not increase output by any measure of output: it merely allows the utility to continue to serve the existing output. That is, infrastructure replacement just duplicates the current service facilities for the most part and serves the same customers. This means that during periods of significant infrastructure replacement (sustainment capital) costs grow more rapidly than output. Thus the TFP is negative. The negative TFP does not mean the utility is inefficient in its investments or in the production of its outputs. It means that the goal of safe and reliable service at the best cost requires additional new investments that permit the utility to replace old equipment with new equipment that over the life of that investment will provide efficient delivery service.[256]

---

[254] Exhibit B-45, Overcast Rebuttal Evidence, p. 49.

[255] Exhibit B-45, Overcast Rebuttal Evidence, p.17.

[256] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.3.

156. Dr. Lowry acknowledged at the hearing that a utility undertaking significant infrastructure replacement will have a negative TFP:

> MR. GHIKAS: Q: Okay, so you aren't disputing the theory or the concept that significant investment in infrastructure replacement or system modernization reliability investment can drive a negative TFP, are you?
>
> MR. LOWRY: A: Not at all. I testified several times in support of capital cost trackers, and I am cognizant of the fact that if the company is engaged in accelerated system modernization, that a capital tracker could be necessary and Fortis has one in its plan.[257]

157. Dr. Lowry has also made the following statement, or a slight variant on it, on at least two occasions in past testimony filed on behalf of utilities in the United States:

> Another short-run determinant of TFP growth is the intertemporal pattern of expenditures that must be made periodically but need not be made yearly. Expenditures of this kind include those for replacement investment and maintenance. A surge in such expenditures can slow productivity growth and even result in a productivity decline. Uneven spending is one of the reasons why the TFP growth of individual utilities is often more volatile than the TFP growth of the corresponding industry. [Emphasis added.][258]

Dr. Lowry's reference to "productivity decline" means a negative TFP.

Negative TFP for the Gas Industry During the PBR Period

158. There is significant evidence on the record to support Dr. Overcast's assessment that accelerated infrastructure replacement is driving a negative TFP for the gas utility industry, and will continue to do so during the PBR period.[259]

---

[257] T7:1356, l.23-1357, l.7 (Lowry); T7:1359, l.18-1362, l.23 (Lowry).

[258] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, pp.12-13 (State of Maine Public Utilities Commission, Central Maine Power Company (Docket No. 2007-215)), pp.85-86 (Vermont Public Service Board in the matter of Central Vermont Public Service (Docket No. 7336)); T7:1357, l.8-1359, l.17 (Lowry).

[259] Exhibit B-45, Overcast Rebuttal Evidence, p.1,7 Black & Veatch's 2012 and 2013 client survey results reinforced that the issues of reliability and aging infrastructure were high priority issues for gas and electric utility executives.

159. First, utility data from recent years, and industry forecasts of infrastructure investment, demonstrate massive investment in infrastructure that will not add customers or capacity:

- The American Gas Association ("AGA") has reported that investment in critical gas industry safety infrastructure is expected to be in the range of $7 billion per year over the next ten years.[260] This industry forecast covers the PBR period.

- Dr. Lowry's own data and calculations for the gas industry showed that accelerated main replacement was occurring over the period of 2007 through 2011 (mains represent the majority of the capital cost for a gas distribution utility). The average change in real investment for the years 2007 through 2011 was 77% higher than the average change for the years prior to 2007.[261] Although Dr. Lowry's methodology masks the impact of infrastructure replacement (because he uses accounting depreciation to reduce the service value (inputs) of existing capital assets), his data contained occurrences that can only be explained by investment in types of infrastructure that do not generate additional outputs. Some gas utilities in Dr. Lowry's sample added tens of millions of dollars in plant in a particular year without adding *any* net miles of main.[262]

160. Second, Dr. Overcast's assessment is also supported by the proliferation since 2007 of special rate mechanisms designed to facilitate gas utility investment in infrastructure that does not generate additional outputs. He explained that these mechanisms implicitly recognize the declining productivity of capital, in that they "supplement the revenue

[260] Exhibit B-45, Overcast Rebuttal Evidence, p.17.

[261] Provided in response to FEI Exhibit C1-16, FEI/FBC-CEC (Lowry) IR 1.3.26; Exhibit B-45, Overcast Rebuttal Evidence, p.18.

[262] Exhibit B-45, Overcast Rebuttal Evidence, p.25.

requirement of utilities with approved programs in recognition of the higher cost of production associated with replacing the infrastructure."[263]

161. Dr. Overcast illustrated the link between accelerating infrastructure replacement and the proliferation of special rate mechanisms by referencing the 2013 National Association of Regulatory Utility Commissioners ("NARUC") "Resolution Encouraging Natural Gas Line Investment and the Expedited Replacement of High Risk Distribution Mains and Service Lines".[264] NARUC was explicit in the Resolution regarding the impetus for the resolution and what it hoped to achieve by passing it. It confirmed Dr. Overcast's evidence:

> WHEREAS, Many States and distribution utilities are undergoing significant pipeline replacement programs to replace aging pipe, and
>
> WHEREAS, Many distribution companies are being proactive about replacing their aging pipelines through a risk based approach focussing on prioritizing safety, asset replacement, and rate impact, and
>
> WHEREAS, Alternative rate-recovery mechanisms may help expedite the replacement and expansion of the pipeline systems by promoting more timely rate recovery for investments in infrastructure, safety and reliability, and
>
> WHEREAS, Alternative rate recovery mechanisms may help eliminate near-term financial barriers of traditional ratemaking policies such as "regulatory lag" and promote access to lower cost capital, and
>
> WHEREAS, The adoption of alternative rate policies may be very effective for advancing critical safety and reliability infrastructure upgrades; and…

The NARUC resolution called for "regulators and industry to consider sensible programs aimed at replacing the most vulnerable pipelines as quickly as possible along with the adoption of rate recovery mechanisms that reflect the financial realities of the particular utility in question". Dr.

---

[263] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), pp.3-4.

[264] NARUC includes representation from every US state regulator. The Resolution was referenced by Dr. Overcast and was put to Dr. Lowry in cross-examination. Exhibit B2-27, pp.119-120.

Lowry acknowledged that the facts stated in each of the above recitals are true, and that NARUC is not in the habit of making resolutions for no reason.[265]

162. The AGA, like Dr. Overcast and NARUC, associates special rate mechanisms with the fact that "while investments made to serve new customers or to deliver additional volumes of gas generate additional revenue, expenditures made to refurbish or to replace aging infrastructure do not produce incremental revenue." [266] (Re-phrased in TFP terms: refurbishment and replacement of assets requires additional inputs without generating additional outputs.)

163. The AGA reported in 2013 that the use of special rate recovery mechanisms had tripled and become widespread since 2007, the first year of Dr. Overcast's TFP measurement period:

> In 2007 when the AGA published its first report on infrastructure cost recovery methods, 15 natural gas utilities in 11 states serving 8 million residential natural gas customers were using innovative rate structures that allowed them to modify tariffs and recover the costs of investments in utility replacement incurred between rate cases. Since that time, the use of these advanced regulatory mechanisms has tripled. Today, 47 utilities in 22 states serving 24 million residential natural gas customers are using full or limited special rate mechanisms to recover their replacement infrastructure investments, and 5 utilities have mechanisms pending in another state and the District of Columbia. Ten states have enacted legislation or issued generic regulations that give utilities in three additional states the authority to implement these mechanisms. A further 14 utilities in 7 states are recovering these investments using rate stabilized tariffs. Together, these regulatory programs are helping natural gas utilities maintain safe and reliable service to more than 30 million of the nation's 65 million residential natural gas customers.[267]

---

[265] T7:1369, l.6-1372, l.23 (Lowry). Dr. Lowry agreed that special mechanisms are put in place because their rate recovery mechanisms aren't equipped to handle significant asset replacement investments, so they need a special rate mechanism: T7:1370, l.25-1371, l.3 (Lowry).

[266] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.122.

[267] "Natural Gas Rate Round Up", Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, pp.121-122. Dr. Lowry indicated that he had no reason to doubt the accuracy of the information: T7:1374, l.9-1377, l.10 (Lowry).

The map included in the AGA publication showed the extent to which the use of such rate mechanisms had blossomed in the space of only a few years. Over 80% of the gas utilities in Dr. Lowry's sample (52 of 64) are located in states that already had some sort of recovery mechanisms by June 2012.[268] He agreed that the proliferation of rate mechanisms is due to there being "some acceleration" in significant infrastructure that is not producing revenues.[269]

164. Dr. Lowry's past testimony before other regulators provides further evidence that North American gas utilities are investing heavily in gas infrastructure replacement. Dr. Lowry has been retained by a number of utilities in recent years to support their applications for approval of alternative rate mechanisms intended to facilitate capital investment that do not directly result in increased revenue generation. In testimony filed in 2011, for instance, Dr. Lowry discussed how "…older facilities were often built with cast iron and/or bare steel, materials which today entail high maintenance costs and raise safety concerns. Expedited capex cost recovery helps gas distributors accelerate the replacement of these old facilities."[270] He gave evidence that "many gas distributors have capex cost recovery mechanisms", and had even included a map of the U.S. showing widespread use of such mechanisms throughout the country.[271]

165. Dr. Lowry, in his written evidence, was critical of Dr. Overcast for suggesting in his TFP Reports that TFP was more likely to be negative during the PBR period due to the significant infrastructure replacement taking place. He suggested that Dr. Overcast's "statements and assertions about empirical trends…are not backed up by facts".[272] However, Dr. Lowry's evidence evolved considerably during the course of the oral hearing, as he was confronted with more and more evidence:

---

[268] "Natural Gas Rate Round Up", Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.121.

[269] T7:1379, ll.16-21 (Lowry).

[270] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.234.

[271] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.234.

[272] FEI Exhibit C1-9-1, Errata to Lowry Evidence, pp.66-67.

- At the outset of his cross-examination, Dr. Lowry would only concede that there were "some" utilities undertaking significant infrastructure replacement in recent years.[273]

- "Some" utilities quickly became "a number of utilities" in his sample, although he still suggested accelerated system modernization was mostly confined to utilities in the eastern U.S.[274] For the other utilities, his response was "I don't know that it has" and "I am not aware that it has and Dr. Overcast has provided no numbers to that effect", rather than denying that it is occurring.[275] He gave an example of a Denver utility being newer; however, the Denver based gas utility, along with other western U.S. utilities, has a full rate mechanism in place to facilitate capital investments that do not generate outputs.[276]

- After Dr. Lowry was presented with (a) the NARUC resolution (he confirmed each recital), (b) the AGA document (he did not take issue with any of it), and (c) his prior evidence in which he had said that "many" gas utilities had special rate mechanisms and had provided a map illustrating the breadth of coverage throughout the U.S., Dr. Lowry stated: "I haven't disputed that there are many gas distributors that are engaged in accelerated system modernization."[277]

166. In summary, there is ample evidence on the record for the Commission to find that accelerated infrastructure replacement is occurring on a significant scale across the North American gas industry. Dr. Lowry's active involvement in recent years in helping utilities address infrastructure replacement challenges perhaps explains why Dr. Lowry carefully phrased his initial criticism of Dr. Overcast in terms of Dr. Overcast *failing to provide any evidence of this phenomenon*, rather than directly refuting the accuracy of Dr. Overcast's

[273] T7:1365, ll.1-7 (Lowry).
[274] T7:1365, ll.13-16 (Lowry).
[275] T7:1365, l.1-1367, l.15 (Lowry).
[276] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.124.
[277] T7:1408, ll.18-20 (Lowry).

discussion as it related to the gas utility industry. The challenges facing gas utilities in North America are so widely acknowledged that to suggest otherwise would not be credible.

TFP for the Electric Industry is More Likely to Be Negative in the PBR Period

167. Dr. Overcast identified a similar recent trend in the electric utility industry of accelerated investments in infrastructure that does not add customers or capacity. He noted that the power industry is expected to invest $20 billion per year for the next ten years in electric T&D infrastructure replacement, which encompasses the PBR period.[278] Dr. Overcast concluded that, in light of the accelerated investments, TFP for the electric industry is more likely to be negative than positive during the PBR period. Although Dr. Lowry was particularly critical of Dr. Overcast's assessment as it related to the electric utility industry,[279] Dr. Lowry's own data and past testimony support it.

168. Dr. Lowry's data shows that from 2007 to 2011 electric utilities increased capital spending by 47%. Only two utilities in his sample had a decline in capital spending over that period. This increase occurred despite the recession in the middle of the period and any impact it might have had on the customer growth measure. The logical explanation of this investment is that infrastructure replacement occurred in this period.

169. Dr. Lowry's criticism as it related to the electric utility industry was again at odds with his own past testimony in other jurisdictions. Dr. Lowry's 2011 testimony on behalf of Potomac Electric Power Company ("PEPCO"), an electric utility based in Maryland, provides the best example of this inconsistency. Notably:

- Dr. Lowry had addressed in his PEPCO evidence "the challenge of chronic under earning due to regulatory lag that PEPCO and many other energy distribution utilities face today under traditional approaches to regulation like that currently

[278] Exhibit B-45, Overcast Rebuttal Evidence, p.17.

[279] FEI Exhibit C1-9-1, Errata to Lowry Evidence, p.68.

used in Maryland."[280] [Emphasis added] PEPCO's challenge, according to Dr. Lowry, had been caused by the fact that PEPCO "plans a large and sustained increase in non-revenue producing capital spending (capex) in order to modernize its infrastructure."[281] He had also referred to the challenge facing PEPCO as "its accelerated modernization program to improve reliability…".[282] Even the name of the rate mechanism that Dr. Lowry had recommended - a "Reliability Investment Recovery Mechanism" - left no doubt as to the type of capital expenditures being addressed.

- Dr. Lowry had explicitly noted in his 2011 PEPCO evidence that the accelerated modernization and infrastructure replacement facing PEPCO was a widespread phenomenon in the electric utility industry, as well as among gas utilities. At various points in his testimony, Dr. Lowry had stated, for example:

> Chronic under-earning is problematic today for many gas and electric power distributors that operate under traditional approaches to regulation. Various Altreg measures are in use around the country which help to mitigate under-earning while preserving regulatory oversight and incentives for efficient management.[283]
>
> …
>
> Recent precedents for expedited CAPEX recovery mechanisms for electric and gas utilities are summarized in Figure 6. It can be seen that that there are precedents in numerous states, including the neighboring states of Pennsylvania, New Jersey, Virginia, and West Virginia. Those for power distribution CAPEX most commonly to recover the cost of AMI or more general accelerated

[280] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.177, ll.8-12.

[281] And the issue PEPCO was facing is described in Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.178, ll.10-13; p.177, ll.18-23, p.179, ll.10-13.

[282] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.179, ll.9-13.

[283] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.178, ll.4-9.

> modernization programs that improve reliability. [Emphasis added.][284]

Dr. Lowry's reference to "general accelerated modernization programs" is a clear reference to infrastructure replacement. Investments in AMI (automated meter reading) are akin to asset replacement programs in the TFP context because AMI requires an increase in inputs without increasing outputs (i.e., the number of customers or capacity).[285]

- Figure 6 in Dr. Lowry's PEPCO evidence depicted graphically the significant number of U.S. states that had capex recovery mechanisms by 2011. They represented more than half of the country, and most of those mechanisms applied to electric utilities or both gas and electric utilities. One third of the utilities in Dr. Lowry's electric TFP sample in this proceeding already had cost recovery mechanisms at the time Dr. Lowry prepared his PEPCO evidence in 2011.[286] More states have introduced such mechanisms since that time.[287]

170. Dr. Lowry's critique of Dr. Overcast for drawing comparisons between what is occurring in the electric industry in terms of infrastructure replacement and the gas infrastructure replacement (a comparison Dr. Lowry twice called "remarkable"[288]) is particularly ironic given that Dr. Lowry had included in his PEPCO evidence (PEPCO being exclusively an electric utility) a significant amount of discussion on what is happening in the gas industry on this very subject. He had identified all of the jurisdictions in which gas mechanisms were being implemented, and had included them in his map of the U.S. He had then expressly drawn an analogy between what is occurring in the two industries, stating "I believe these gas and water

---

[284] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.234, ll.6-13.

[285] T7:1410, ll.14-20 (Lowry).

[286] This can be seen by cross referencing the list in Table 4 from Dr. Lowry's evidence in this proceeding, with Table 4 in the PEPCO evidence found on p.230 of Exhibit B2-27.

[287] T7:1411, ll.17-20 (Lowry).

[288] FEI Exhibit C1-9-1, Errata to Lowry Evidence, p.68.

utility precedents are quite relevant to the consideration of PEPCO's proposal."[289] It is difficult to see how Dr. Overcast's evidence could be so "remarkable" when Dr. Lowry had also concluded in 2011 that the circumstances facing gas and electric utilities were analogous.

171. Dr. Lowry's evidence in the PEPCO case wasn't an anomaly. His recent testimony filed with the Washington State regulator on behalf of Avista Corporation provides another example of Dr. Lowry's recognition of the link between infrastructure replacement in the electric industry and the recent proliferation of special rate mechanisms. In that case, Dr. Lowry had advocated for a special rate mechanism for Avista to address accelerated investment in infrastructure that would not generate new revenue (i.e., it didn't serve any new customers):

> Many utilities today face operating conditions that differ materially from those that gave rise to traditional regulation. Cost growth is much more likely to outpace growth in billing determinants. The problem is aggravated to the extent that a utility must content with either high capex requirements or unusually sluggish or negative growth in average use. Utilities that must contend with these challenges under traditional regulation are likely to file annual rate cases and receive rate adjustments that are uncompensatory.
>
> Certain kinds of capex aggravate utility financial stress. Some CAPEX programs involve assets that generate no revenue automatically and are not "lumpy" so that assets of smaller but still sizable value become used and useful each year over a sequence of years. Examples include programs to replace aging distribution and transmission assets, to make small refurbishments to generating plants, and to install generation emissions equipment.
>
> …
>
> Capex [for Avista] is well in excess of depreciation expenses and the rate base is growing briskly. As discussed more fully in the testimony of Mr. DeFelice, CAPEX is forecasted to continue at high levels well beyond 2013, the year that new rates will be in effect. A sizable portion of the CAPEX generates no new revenue

[289] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.235; T7:1409, ll.7-13 (Lowry); T7:1411, l.17-1412, l.7 (Lowry).

> automatically and is producing a stream of newly used and useful assets over several years. [Emphasis added.][290]

172. At the hearing, Dr. Lowry emphasized that some of the rate mechanisms in the electric industry have been implemented to address initiatives such as AMI. Whether or not these mechanisms are intended to facilitate AMI or more traditional infrastructure replacement doesn't change the fundamental point that Dr. Overcast has made; as indicated previously, neither type of investment adds outputs commensurate with the increased inputs. Dr. Lowry agreed with the proposition that "the issue with AMI, just as with accelerated modernization, is that they are capital expenditures that are not generating revenues *per se*. They're serving the same outputs."[291]

173. In summary, there is a sound evidentiary basis for the Commission to conclude that the electric utility industry is experiencing the types of accelerated investment that will continue to drive a negative TFP during the PBR period.

Summary on Infrastructure Replacement

174. There is a level of imprecision in any TFP estimate, but the significant accelerated infrastructure replacement occurring in the electric and gas utility industries point to a negative TFP as measured by Dr. Overcast, not a significant positive TFP like the one calculated by Dr. Lowry. Dr. Overcast summed up this point nicely:

> And you know, I am not saying my estimates are perfect, I wouldn't go that far, and I don't think -- just as a matter of practicality, nobody's estimates are perfect in this concept because TFP, even in the literature, if you read the literature it says it is a measure of our ignorance, because it says we can't explain why outputs and inputs are different with any kind of precision.…
>
> I am not so bold as to say my judgment is perfect here, but I think you have to look beyond that, and you have to say, is the sign reasonable? The sign on my estimates are reasonable because it is a period in which utilities have been expending a substantial amount of capital for infrastructure replacement. And

[290] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, pp.257-258, 260-261.

[291] T7:1410, ll.14-20 (Lowry).

> that means that the TFP would be negative because you are increasing inputs faster than you are increasing outputs.[292]

There are other considerations, described below, that support a measured negative TFP in the present circumstances and over the next five years.

(b) PEG's Recent Work in Ontario

175. PEG (the firm for which Dr. Lowry serves as President) recently calculated a negative TFP for the Ontario electric industry. Although the study was based on Ontario electric utilities and used a variant of Dr. Lowry's methodology (which Dr. Overcast does not endorse), the study results lend credence to Dr. Overcast's measured TFPs and FortisBC's proposed X-Factor.

176. The Ontario's 3rd Generation Incentive Regulation (2009-2013) had been based on PEG's measured TFP for the Ontario electric industry of 0.72 per cent. PEG's initial study for the 4th Generation Incentive Regulation (2014-2018), which was based on data up to 2011, had showed a significant decline in measured TFP. It was only slightly positive at that time. When PEG updated its 4th Generation study in September 2013, its measured TFP results declined "to -0.33% or -0.27% if savings from OPA conservation programs are added back into output growth."[293] The downward trajectory in PEG's measured TFP over time is as notable as their recent negative TFP results.

177. PEG identified in its September 2013 report "several reasons why PEG believes a negative productivity factor would not be appropriate in 4th Gen IR". Taking all of those factors into account, PEG recommended a productivity (X) factor of "no lower than zero".[294] PEG assigned stretch factors to different cohorts of utilities in the range of zero to 0.6%. The result is that PEG's recommended X-Factors were below FortisBC's proposed 0.5% X-Factor for all

[292] T3:572, l.24-574, l.3 (Overcast).

[293] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.168.

[294] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, pp.169-171.

utilities other than electric distributors whose actual costs are more than 15% above the costs predicted by PEG's cost benchmarking model (in which case the X-Factor was to be only slightly higher, at 0.6%). The average was 0.3%.[295] Dr. Overcast commented that "you would have expected with the history of PBRs here in British Columbia that both of the ---both Fortis Gas and Fortis Electric would be on the low end of that, as opposed to the high end."[296]

178. The results of the 2013 update prepared by Dr. Lowry's colleagues at PEG for the OEB are important to keep in mind in considering Dr. Lowry's characterization of Dr. Overcast's study as a "lowball productivity estimate", and his rather confident assessment that: "One cloud on the horizon [for the "future of PBR in Canada"] is the increasing tendency of Canadian utilities to hire inexperienced consultants to file productivity reports with results that are markedly at variance with those from long-time practitioners such as NERA and PEG."[297] In particular:

- In comparing the results of Dr. Lowry's TFP study in this case, PEG's recommended X-Factors for the OEB , and Dr. Overcast's study, it is Dr. Lowry's much higher TFP results that stand out as anomalous.[298] Dr. Lowry's response to this observation was to disclaim personal responsibility for his colleagues' work: "But let me make very, very clear that I had nothing to do with that [PEG's Ontario] study. The way our company is structured, the person in charge of that is completely independent of me, so."[299] Throwing his colleagues under the proverbial bus isn't an answer to the observation, and it certainly does little to

[295] Dr. Overcast explained that it is not analytically correct to associate higher costs with lower efficiency, as this benchmarking exercise implicitly assumed: T3:388, l.2-392, l.17 (Overcast).

[296] T3:512, ll.1-5 (Overcast).

[297] FBC Exhibit C6-13, BCSEA-CEC (Lowry) IR 1.11.2.

[298] Although both Dr. Overcast and PEG in Ontario have adjusted negative TFP values upwards to arrive at an X-Factor recommendation of zero and "no lower than zero", respectively, there is no theoretical impediment to having a negative X-Factor. Dr. Overcast and PEG identified instances where that can be appropriate, and where it has been done (Australia and the UK). Exhibit B-45, Overcast Rebuttal Evidence, p.19, Schedule HEO-1 Rebuttal; Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.169 (PEG Report to OEB).

[299] T7:1400, ll.1-12 (Lowry).

support Dr. Lowry's desire to preserve a TFP consulting monopoly for "long-time practitioners such as NERA and PEG".

- As will be discussed later, a key point that Dr. Overcast has made in this proceeding - which Dr. Lowry continues to dispute - is that Dr. Lowry's omission of a capacity-based measure of outputs biases TFP upwards, as does reliance on volumetric measures. PEG's September 2013 update incorporates a capacity-based measure of output.

- NERA's work in the AUC proceeding in 2012 is hardly compelling support for preferring the work of "long-time practitioners" to protect "the future of PBR in Canada". Dr. Lowry offered at the hearing that NERA's analysis had been riddled with errors, and that NERA had even been reluctant to acknowledge the errors except where they were so obvious that it could not be avoided.[300] Dr. Overcast addressed some of the most significant errors in NERA's analysis in his review of PBR in other jurisdictions.[301]

179. Dr. Lowry's suggestion that Dr. Overcast is "inexperienced" is only accurate if one considers TFP measurement to be an academic exercise in rote calculation. Dr. Overcast may not have performed a TFP study before, but it should be self-evident from his academic credentials, his written testimony and his performance at the hearing that: (a) he not only understands productivity theory, but is aligned with the latest writings on the topic;[302] (b) he understands how Dr. Lowry has calculated TFP and the data and assumptions Dr. Lowry has employed; and, (c) has a deep knowledge of how utilities actually operate. This last point is particularly important. Even Dr. Lowry admits that the value of his work depends on the assumptions he makes truly reflecting reality, and Dr. Overcast has much greater experience in

[300] T6:1341, ll.11-21 (Lowry).

[301] FEI Exhibit B-1-1, FEI Application, Appendix D1, Comparison of Recent Performance-Based Regulation for Distribution Utilities in Canada.

[302] This is discussed further in the next section. See, for instance, the discussion regarding Dr. Deiwert and Dr. Deiwert's criticism of Dr. Lowry's approach in a utility context.

that regard.[303] Dr. Overcast has succeeded in taking an academic exercise (TFP analysis) and making it relevant to the real circumstances faced by regulated utilities in North America. FortisBC submits that, contrary to Dr. Lowry's assessment, the participation of an accomplished individual like Dr. Overcast - who has the credentials to bridge the gap between academic analysis and the real world using his practical understanding of the utility business - is a much-needed development.

(c) Comparison to Forecasts for the PBR Period

180. The Companies included in their respective Applications (sections C3 and C4 for FEI and sections C4 and C5 for FBC) O&M and capital forecasts for the PBR Period. These forecasts are not cost of service forecasts akin to the forecasts used in the last revenue requirement applications, but they are indicative of the future trends and challenges that the Companies expect to face during the PBR Period. The reasonableness of FEI's proposed X-Factor of 0.5% is supported by the fact that the proposed formula results in a cost and investment trajectory for combined O&M expense and capital investment for both FEI and FBC that is lower than what is reflected in the long-term forecasts.

- ***FEI:*** Section B7 of the FEI Application demonstrates that the rates arising from the PBR formulas (the combination of proposed 0.5 per cent X-Factor and the proposed composite inflator) compare very favourably to FEI's forecast. When the O&M and capital allowed under the PBR formula for FEI are examined together, the total is lower than what has been forecasted by FEI under both scenarios in every year of the PBR term.[304] The formula will lead to average delivery revenues that are $29 million or 1.2 percent lower than the average rates under the cost of service model.[305] When FEI's allowed O&M and capital are examined separately, the allowed expenditures under the PBR formula track more closely for capital than it does for O&M. While the capital allowed under

[303] T7:1390, l.9-1394, l.8 (Lowry).

[304] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, p.67, Figure B6-4.

[305] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, p.83.

the PBR formula is lower than the high construction cost forecast in most years, it is also higher in some years than that forecasted when compared to the low construction cost scenarios. The allowed O&M expenditure under the PBR formula falls significantly below what has been forecasted over the PBR Period.[306]

- ***FBC*****:** Section B7 of the FBC Application also shows a favourable comparison. When the O&M and capital allowed under the PBR formula for FBC are examined together, the total is lower than what has been forecast by FBC in every year of the PBR term, with the exception of 2017. Average capital expenditures under the formula are 2.7 percent lower than the average revenues under the COS model.[307] Formula-driven O&M closely align with the forecast O&M.[308]

181. The Companies will have to find productivity improvements during the PBR Period in order to offset the costs that they are forecasting. This evidence supports that the proposed PBR Plan, including the X-Factor, provides an appropriate incentive.[309] Since these O&M and capital forecasts do not directly affect the determination of the PBR formula or 2014 rates, FortisBC will respond in its Reply Submission if interveners choose to take issue with aspects of the forecasts in their submissions.

(d) FortisBC Utilities' History of PBR Suggests Stretch Factor Lower Than 0.5%

182. The reasonableness of the proposed X-Factor of 0.5% is also supported by the fact that FEI and FBC already have a long history under PBR. FBC has been under PBR for 14 of the last 17 years.[310] FEI has been under PBR for 10 of the last 15 years. Drs. Overcast and Lowry are united with respect to the importance of considering diminished ability to identify

---

[306] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, pp.66-67.

[307] FBC Exhibit B-1-6, FBC Application Evidentiary Update October 18, 2013, p.59.

[308] FBC Exhibit B-1-6, FBC Application Evidentiary Update October 18, 2013, p.54.

[309] FEI Exhibit B-1-5, FEI Application Evidentiary Update February 21, 2014, pp.66-67; FBC Exhibit B-1-6, FBC Application Evidentiary Update October 18, 2013, p.60.

[310] T3:394, l.19-395, l.1 (Swanson).

savings after an extended period of PBR. Their respective recommendations for an appropriate stretch factor are less than the stretch factor incorporated in the proposed 0.5% X-Factor.

183. Dr. Overcast described the principle that it is harder and harder to find new efficiency gains the longer you have been in PBR as "an accepted theoretical principle as well as just being a factual matter as you deal with the operation of a utility."[311] He elaborated:

> While utilities with no experience with PBR may have numerous opportunities to improve efficiency at relative minor costs, this so called "low hanging fruit" has been captured by FBC and FEI over earlier PBR periods. Basic economics supports the conclusion that after numerous years under PBR Plans, the available efficiency gains are more difficult and costly to obtain. This is known as the law of diminishing returns and applies in the management and operation of electric and gas utilities.[312]

184. Dr. Lowry recommended an explicit stretch factor of 0.2%, which is smaller than Dr. Overcast's implicit stretch factor. When asked why he recommended a stretch factor of 0.2%, Dr. Lowry responded:

> Dr. Lowry has performed incentive power research for many years which estimates the expected cost efficiency growth of utilities under alternative, stylized regulatory systems. This research has been funded by numerous clients, including Canadian utilities and regulatory agencies. Based on this research, Dr. Lowry has found that a modest improvement in the incentive power of a regulatory system is likely to accelerate cost efficiency growth by around 20 basis points in the long run.
>
> Dr. Lowry explained in his testimony that the incentive power of the regulatory systems proposed by the Fortis companies is likely to be only modestly stronger than the incentive power of the regulatory systems of the sampled utilities. Since, additionally, there is no reason to believe that the utilities are superior or inferior cost performers, stretch factors of 0.20% are indicated.[313]

---

[311] T3:393, ll.4-12 (Overcast).

[312] Exhibit B-45, Overcast Rebuttal Evidence, p.17. See also: T3:504, l.13-505, l.18 (Overcast). Dr. Lowry, in his testimony before the Maine regulator, accounted for the utility's past time under PBR in arriving at a stretch factor recommendation of 0.2%: Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.9.

[313] FBC Exhibit C6-13, BCSEA-CEC (Lowry) IR 1.7.1.

185. The logic of diminishing returns holds true in the context of the FortisBC Utilities:

- FBC achieved 27.5% of "productivity improvement factors" over the past 15 years. The increased productivity is embedded in the business.

- In the last FEI PBR, the three gas utilities (FEI, FEVI and FEW) were integrating as part of the Utilities Strategy Project. This integration was the source of significant savings under the PBR. The circumstances today are different. The gas utilities are fully integrated.[314]

- FEI and FBC have been under common ownership for several years, and the obvious savings from management integration have already been achieved.[315] There are fewer integration opportunities with gas and electric utilities than among gas utilities, simply given the differing nature of the business. FortisBC's evidence is that there are obstacles to further savings from integration:

> Further opportunities may emerge and will be evaluated depending on the circumstances and potential benefits to customers. Future integration opportunities are expected to be more complex and dependent on the Company's ability to overcome some challenges. These challenges include concerns raised by unions representing gas and electric employees around shifting of unionized work from one entity to another, and the need to transition to common IT platforms before more harmonization of business processes can occur. Differences in the nature of the gas and electric operations also pose challenges and limit the breadth of opportunities available. While the Company will continue its efforts to investigate productivity opportunities, future progress is expected to be considerably slower given the highlighted challenges, and may require an upfront investment in IT systems or other initiatives to achieve significant and sustainable savings.[316]

---

[314] T2:258 l.20-259, l.4 (Roy).

[315] T2:258 l.20-259, l.4 (Roy); T3:395 l.7-396, l.4 (Swanson).

[316] FEI Exhibit B-1, FEI Application, p.13. With respect to FBC, FBC Exhibit B-1, FBC Application, p.14.

186. Mr. Swanson referenced the extent of past productivity achievements and summed-up as follows regarding how they should be accounted for in the X-Factor:

> So as time goes on, and as you go further and further down the road of PBR and British Columbia where we are a lot further than most jurisdictions are with PBR, your opportunity does shrink. And when we put forward our expectation of a stretch factor for productivity improvements, we do it in light of the fact that we've already achieved many years of productivity and that's already taken from the business. We can't then go take it again because it's no longer there. Those positions are no longer there, those employees are no longer there.[317]

187. On the whole, there is a strong theoretical and practical basis for the Commission to conclude that the proposed 0.5% X-Factor incorporates an appropriate stretch factor.

D. DR. LOWRY'S CALCULATED TFP IS OVERSTATED

188. Dr. Lowry, like Dr. Overcast, used appropriately large utility samples and reliable data sources, in calculating TFP (or MFP, as Dr. Lowry calls it[318]). However, there are significant differences in the way in which Drs. Overcast and Lowry performed their calculations. Dr. Overcast identified a number of reasons why Dr. Lowry's approach gave rise to measurement error when applied to the utility industry and resulted in upward bias in his measured TFP. In this section, we highlight several of the most material issues. In particular:

- Dr. Lowry's long study period gave insufficient weight to the recent acceleration of infrastructure replacement occurring in the gas and electric industries, and thus biased TFP upwards.

- Dr. Lowry's output measures did not align with the widely-recognized drivers of utility costs, and biased TFP upwards.

---

[317] T2:325, l.17-326, l.1 (Swanson).

[318] Dr. Overcast explained that, for all practical purposes, they could be treated as being synonymous: T4:860, ll.11-26. Dr. Lowry agreed: T7:1347, l.16-1349, l.15 (Lowry).

- Dr. Lowry's method of calculating inputs incorporated a number of assumptions, either explicitly or implicitly, that were not realistic and biased TFP upwards.

- Dr. Lowry did not "calibrate" his TFP results downwards, although his approach required it and he had calibrated the results of his previous work for utilities.

The Commission should find that Dr. Lowry's methodology did not yield results that are meaningful in light of the real circumstances facing utilities. If Dr. Lowry's methodology is to be used, then his recommended X-Factors must be adjusted downwards to account for the fact that his TFP analysis significantly overstated TFP for the electric and gas industries. The Companies would not have a reasonable opportunity to earn a fair return if the Commission were to accept Dr. Lowry's recommendations at face value.

(a) Understanding Dr. Lowry's TFP Methodology

189. Dr. Lowry employed an index-based approach. The derivation of the index for capital and O&M is a method for developing a measure of change in the levels of various economic variables. A traditional index-based TFP approach like the one Dr. Lowry used will not yield a reliable estimate of future productivity gains for the industry to the extent that business conditions facing utilities do not match the assumptions inherent in the index-based approach. The key explicit and implicit assumptions that provide the foundation for Dr. Lowry's approach (assumptions which, during the hearing, Dr. Lowry insisted on characterizing as "approximations of reality")[319] do not approximate reality very well. Given how Dr. Lowry has employed the assumptions in his formulae, the biases in individual assumptions compound, rather than cancel each other out. They result in TFP numbers for the gas and electric industries that are much too high, i.e., his method makes the industries appear significantly more productive than they really are. Any X-Factor based on Dr. Lowry's estimated TFP would embed an expectation of productivity levels that exceeds what FEI and FBC can reasonably be

[319] Dr. Lowry's reluctance under cross-examination to acknowledge that he made "assumptions" was particularly baffling given that he used the word "assumption" in the very passages from his written testimony being referenced, and kept using the term "assume" unintentionally in his verbal responses. T7:1390, l.13-1392, l.2 (Lowry); T7:1435, ll.3-18 (Lowry).

expected to achieve during the PBR period. As discussed earlier in Part 2 of this PBR Submission, Dr. Lowry's I-X formula would require that the Companies achieve over four times the efficiency savings than those already proposed by the Company.[320]

(b) Long Measurement Period Understates Recent Infrastructure Replacement

190. Dr. Lowry used a study period of 1998-2011 for gas utilities and 2002-2011 for electric utilities. Since his TFP calculations are only affected by the first and last year of in his study period,[321] Dr. Lowry's long study periods gave insufficient recognition to the recent acceleration of infrastructure replacement that is driving a negative TFP for both the electric and gas utility industries. It introduced an upward bias in the measurement of TFP for the years covered by the proposed PBR Plan.

191. FortisBC discussed earlier in Part 4 the evidence that investment in infrastructure replacement has recently accelerated for both gas and electric industries. In terms of the timing of these developments, it is notable that the use of special rate recovery mechanisms for the gas industry has tripled since 2007. Given that the purpose of rate recovery mechanisms is to prompt investments in replacement infrastructure, it is reasonable to expect that investments would be increasing along with the proliferation of the mechanisms. Dr. Lowry conceded that the tripling of rate mechanisms "probably is indicative of some up-tick [in infrastructure replacement] since 2007."[322]

192. Dr. Overcast acknowledged that the most recent five-year period included the years of 2008 and 2009 when economic conditions were poor, and that this could reduce output below what might be expected in normal economic conditions. However, Dr. Lowry has significantly overstated the importance of this point.[323]

---

[320] Exhibit B-45, Overcast Rebuttal Evidence, p.3.

[321] Dr. Lowry stated at the hearing that this was the effect of using logarithmic calculations for change: T7:1428, ll.1-9 (Lowry).

[322] T7:1419, l.17-1420, l.14 (Lowry).

[323] T7:1494, l.12-1496, l.17 (Lowry).

- Whereas a volumetric measure of output would be significantly influenced by economic circumstances (because many people and businesses use less gas or electricity when the economy is bad), Dr. Overcast isn't using volumetric measures of output because volume is not a driver of distribution and transmission costs. Customer and capacity output measures -- the proper measures of output for utilities - would exhibit much greater stability through economic cycles. Dr. Overcast stated: "…because the measures of output do not suffer from volatility caused by weather or by the business cycle directly, there is much less need for using long historical periods to estimate TFP for use with a much shorter regulatory control period."[324] The customer and capacity measure are also going to be quite stable because the number of new customer additions and amount of new capacity added in a year represents only a tiny fraction of the overall customer base or total system capacity.[325] So, for example, even if customer growth rates were to change significantly in a given year, the impact relative to the utility as a whole would be negligible.

- Dr. Lowry's own data demonstrates that the effect of the recession on capital spending was muted. From 2007 to 2011 electric utilities increased capital spending over the prior sample period by 47%. Only two utilities in his sample had a decline in capital spending over that period, despite the recession in the middle of the period.

193. Even accounting for the unusual economic conditions in 2008 and 2009, the very significant uptick in infrastructure replacement across North America in recent years still makes Dr. Overcast's five year study period more representative of the future period than the years prior to 2007. Dr. Lowry's long study period introduced upward bias in his TFP estimates.

---

[324] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.10.

[325] For instance, for FEI the number of net customer additions in 2012 was 4,743, as compared to a total customer base of 839,040. This represents a change of 0.56%: FEI Exhibit B-1, FEI Application, Appendix E2.

(c) Dr. Lowry's Choice of Output Measures Introduces Upward Bias in TFP

194. Since TFP is the change in outputs minus the change in inputs, the choice of output measures a fundamental determinant of TFP. Drs. Overcast and Lowry agree that output measures must be related to what is driving utility costs, but they disagree on what drives utility costs. The use of capacity as a cost driver for transmission and distribution plant has long been settled.[326] FortisBC submits that Dr. Lowry's decision to exclude a capacity-based measure from both of his studies added upward bias to his TFP calculations, as did his belated introduction of a throughput-based measure for calculating TFP for the electric industry.

Measure of Outputs Must Reflect Real Cost Drivers

195. Output measures are representative of a regulated firm's cost drivers. Ideally, a comprehensive set of cost drivers should be used to best capture the scale of the utility activities and services that the company undertakes.[327] Dr. Lowry agrees that outputs should reflect cost drivers.[328] Drs. Lowry and Overcast also agree that a distribution system does not produce gas or electricity as an output; its output is related to the physical systems that deliver gas as opposed to the gas itself.[329]

Dr. Lowry's Omission of Capacity Measure Introduced Upward TFP Bias

196. Dr. Lowry's decision to exclude a capacity-based measure of output was analytically incorrect based on the drivers of utility costs, and resulted in his measured TFP for gas and electric industries being overstated.

197. Dr. Overcast explained that, based on his research and experience, costs for natural gas distribution companies are mainly caused by a combination of customers, density,

---

[326] FEI Exhibit B-11, BCUC-FEI IR 1.30.1.

[327] FEI Exhibit B-1, FEI Application, pp.49-50.

[328] T7:1445, ll.2-12 (Lowry).

[329] T7:1445, l.13-1446, l.5 (Lowry).

the age of assets and design day capacity served by the utility system.[330] It is widely understood in the context of COSA studies that, for both electric and gas utilities, capacity is a significant driver of distribution and transmission function costs.[331] Dr. Overcast stated:

> And if you've ever done a cost of service or seen a cost of service proceeding, you know that most of the costs are driven by either capacity or customers. And capacity may be defined in different ways. In gas it's usually the design day capacity. In electric there's really a bunch of different capacities because you would use some kind of coincident peak for transmission, and when you get down to distribution you're using an NCP and maybe a customer non-coincident peak. And so the two components, customer and capacity, are the things that drive costs, so that's why they were used as the measures of output in the [Overcast] study.[332]

Since transmission and distribution assets are costly to install, they are sized to meet the expected load growth over their life at the time of initial installation on the assumption that ongoing load growth will consume the remaining capacity.[333] This is the essence of the concept of lumpy capital additions.

198. Dr. Overcast explained that it was analytically incorrect for Dr. Lowry to omit a capacity-based output measure from his analysis because it meant that Dr. Lowry was using an incomplete specification of outputs:

> By itself, the number of customers does not properly measure the required inputs to produce the different output mix for either electric or gas utilities because it ignores the impact of growth on the requirement for more delivery capacity. No net new customer is ever added to the utility system without the expansion of some elements of capacity. Also, net new customers does not measure the actual number of new facilities required to serve customers. Since

---

[330] In the gas context, the measures used were: Composite Output- Density-Weighted Number of Customers and Capacity; Output- Customers; and Output- Capacity. FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), p.9.

[331] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), pp.2-3.

[332] T4:696, ll.12-24 (Overcast).

[333] FBC Exhibit B-7, BCUC-FBC IR 1.27.1.5.

> the attachment of gross new customers all require new inputs the customer measure does not properly account for new additions.[334]

199. Dr. Lowry's mis-specification of outputs to exclude a capacity measure introduced an upward bias in his measured TFP. Dr. Overcast explained in his Rebuttal Evidence:

> The basic modeling error in the academic model used by PEG is that the measure of output is a change only in the current period output such as the number of customers. The change in input is actually designed to produce output beyond the amount needed in the current period and this is a sound reason for using a measure of capacity as part of the output measure since the capacity input miles of pipe by size allows for an estimate of the physical measure of the input required to produce the output for each firm based on their own operating pressures. (It is important to note that there are two pipe pressures that are important and differ for each utility - the normal operating pressure for a system and the maximum allowable operating pressures.) The marginal cost of the capacity of a transmission line (gas or electric) is the total cost divided by the units of capacity added to the system not the number of customers served or the change in transmission peak demand for the current period. This means that when measuring output as only the current change in customers the marginal or avoided costs would be overstated. This is an example that relates to the measurement of TFP because the measurement of the price using a current index of construction prices is not the basis for the decision to add the extra capacity (the lumpy addition) but rather the minimization of the long-run revenue requirement of the asset using the discounted present value of the stream of revenue requirements resulting from the addition of the asset. <u>It is critical to include the capacity measure of output to avoid the error that the inputs differ based on the combination of outputs (the output mix) and the resulting measure of inputs does not properly explain the level of output resulting in a biased residual that includes a significant measurement error for both inputs and outputs. Unfortunately the PEG study gets neither of these concepts correctly measured and it is impossible to know the measure of the combined error even though we know the capital input error results in a higher TFP because of the underestimate of the change in capital inputs.</u> [Emphasis added.][335]

---

[334] Exhibit B-45, Overcast Rebuttal Evidence, pp.20-21.

[335] Exhibit B-45, Overcast Rebuttal Evidence, p.35.

200. As indicated earlier in this PBR Submission, Dr. Lowry's colleagues at PEG have used a capacity measure in their most recent TFP update in Ontario. The weights that PEG applied in Ontario to customer numbers, system capacity peak demand and retail kWh deliveries (volume) when constructing their output quantity index were 0.606, 0.289, and 0.106, respectively. In other words, PEG assigned the capacity measure almost three times the weight as they assigned to throughput.[336] PEG's adoption of a capacity based measure can only be interpreted as realization that the customer-only output specification still being used by Dr. Lowry is analytically incorrect.

Late Adoption of a Volumetric Measure of Output Compounded Bias

201. Dr. Lowry introduced a volumetric component of his output measure for the electric industry in his second round IR responses, citing the results of further econometric analysis undertaken in the course of responding to IRs. (His work for gas distribution "did not yield any results materially different from that already reported", meaning that he continued to use customers as his sole measure of output.)[337] The addition of a volumetric output measure only added to the upward bias in his measured TFP for the electric industry.

202. Dr. Overcast explained that using volume or throughput as a measure of output for a utility yields incorrect TFP results because throughput is not a driver of the vast majority of utility costs.[338] Volumetric measures are not used in COSA analysis for plant because a change in the level of throughput for an electric utility (or a natural gas distribution utility) does not change the level of fixed costs for the utility delivery function. Dr. Overcast elaborated:

> …there is no reason to believe that the quantity of throughput changes system costs in the short-run or the long-run. Once the system has sufficient capacity to satisfy the various customer peaks (coincident peak, class non-coincident peak and individual customer non-coincident peak) there is no cost associated with increasing or decreasing volumetric measures of delivery for either gas or

[336] Exhibit B2-27, Materials for Cross-Examination of Dr. Lowry, p.146.

[337] Exhibit C1-23, FEI/FBC-CEC IR 2.1.1; T7:1453, ll.4-16 (Lowry).

[338] In a COSA, the cost drivers for a particular function (distribution/transmission/generation) are identified at the stage typically referred to as "classification".

> electricity. Volume is simply not an output of the delivery system and hence has no impact on the measurement of the change in outputs less the change in inputs.[339]

203. Dr. Lowry admitted that in a COSA for an electric or gas utility the costs associated with the transmission function would be classified as being demand related, where demand is a measure of capacity. He also admitted that when an electric company builds a transmission line it is built to accommodate the expected peak load over the long-term. Nevertheless, his position was: "Bear in mind that this is the engineer's view compared to the economist's view. And so it's not that one is automatically more right than the other."[340] In this instance, it is the case that the engineer's view is correct. An economist seeking to identify cost drivers should be basing those drivers on the engineering reality, as is typically done in a COSA (and as Dr. Overcast - an economist and COSA expert - has done).

204. Dr. Lowry's approach of using econometric analysis to identify volume as a utility cost driver is based on flawed logic. Econometric analysis proves correlation, not causation. While a correlation demonstrated by econometric analysis can provide useful information to support or dismiss a hypothesis about causation, it is backwards to use an econometric analysis to identify the hypothesis itself (in this case, his hypothesis that volume might cause costs for utilities).[341] The hypothesis of cause and effect must come first, and must be based on some logic that reflects known facts.[342]

205. Dr. Lowry, in adopting a volumetric measure of output based on the results of econometric analysis, has confused correlation with causation. Dr. Lowry has not identified any logical reason to hypothesize that volume might drive any material costs on a utility distribution system. There isn't one. Volume is not used in COSA analysis to allocate plant. The best that Dr. Lowry could suggest under cross-examination was that volume "might have some role as

---

[339] Exhibit B-45, Overcast Rebuttal Evidence, p.71.

[340] T7:1462, l.3-1465, l.11 (Lowry).

[341] T7:1466, l.26-1467, l.21 (Lowry).

[342] FEI Exhibit B-49, Overcast Supplemental Rebuttal Evidence, pp.1-2.

evidenced by this model right here [his econometric model]" [343] which is less definitive than his IR response had suggested. FortisBC does not dispute that there would be a long-run *correlation* between distribution and transmission costs and energy volumes (kWh), but the increased volumes are not *causing* the increased costs. The correlation exists because energy volumes (kWh) tend to increase in the long-term as customers and capacity are added to the system. It is the addition of customers and capacity, not the added kWh, that is driving the cost.

206. There is upward bias inherent in using kWh as an output measure. As usage (Dr. Lowry's output measure) increases and no investments in plant (input) are required (because volume does not drive transmission and distribution capital investment), TFP will increase.

(d) Input Values are Based on Unrealistic Assumptions and Create Upward Bias

207. Since TFP is the change in outputs minus the change in inputs, the choice of input measures is also critical to TFP study results. Drs. Overcast and Lowry measure inputs differently. As discussed earlier, Dr. Overcast determined, for each year, the actual *ex post* input costs on a utility by utility basis for every utility in his sample, including the utility-specific cost of capital. He used this information to derive a central tendency for each industry. Dr. Lowry, by contrast, determined inputs indirectly, by creating index values for all of the utilities in his sample each year. We focus below on the following notable shortcomings relating to Dr. Lowry's approach to determining labour and capital inputs:

- First, Dr. Lowry's index-based approach incorporates a number of assumptions, either explicitly or implicitly, that are unrealistic and lead to mis-estimation of TFP when applied to the gas and electric utility industries in a way that Dr. Overcast's methodology does not.

- Second, the index that Dr. Lowry used to deflate labour costs reflects a mix of costs that are too high for the utilities in the sample or FortisBC, which results in

[343] T7:1465, ll.12-20 (Lowry).

an input quantity that is too low and a TFP that is too high (i.e., the industry is made to appear more productive in its use of labour than it really is).[344]

- Third, the nominal capital input values are also too low, which further overstates TFP (i.e., the industry is made to appear more productive in its use of capital than it really is) because Dr. Lowry has expressly assumed that:
    - the service value of capital inputs declines on a straight line basis until it no longer has service value, even though utility assets are frequently still in use at full service value long after being fully depreciated on an accounting basis; and
    - there is no net salvage, when utilities actually incur significant net negative salvage for utility plant.
- Fourth, the capital input values are also too low, which further overstates TFP (i.e., the industry is made to appear more productive in its use of capital than it really is) because the index that Dr. Lowry used to deflate capital costs reflects a mix of costs that are too high for the utilities in the sample or FortisBC.

In short, there is a consistent upward bias in Dr. Lowry's assumptions, which leads to TFP being significantly overstated.

Mis-estimation Inherent in Dr. Lowry's Approach

208. Dr. Lowry's approach incorporates a number of assumptions, either explicitly or implicitly, that are unrealistic and lead to mis-estimation of TFP when applied to the gas and electric utility industries.

[344] T4:621, ll.16-22 (Overcast): It may seem counterintuitive for an overestimate of costs to result in an outcome that makes the industry appear more productive than it really is. This results from the fact that Dr. Lowry is using these indexes to deflate costs, and that requires using the index as the denominator in his formula. As a matter of mathematics, dividing by a larger number necessarily yields a smaller outcome.

Assuming Uniform Cost of Capital Introduces Measurement Error

209. The assumption of a uniform capital cost is simply a measurement error that impacts the index measure for all utilities. Since this is an average value the measure is too high for half of the utilities and is too low for the other half. The cost of capital (debt and equity) is a significant cost of operating a utility. Dr. Lowry has used an average capital structure and WACC. Since capital prices are determined administratively by regulation and are not based on the marginal cost of capital but on the embedded cost of capital, each utility has its own capital structure and its own cost of debt and equity.[345] The use of a common capital structure and common debt and equity costs is arbitrary and inconsistent with the economics of each utility in the TFP study.

210. By using an arbitrary capital price to determine capital quantity, the capital quantity "cannot reflect either the actual physical quantity of capital or even a reasonable proxy value for input mix of each utility in the sample." The issue is that it is actual cost of capital that enters into the decisions to invest in capital. The distortion of capital price causes utilities to choose both a different mix of capital and different timing of investments. Thus, dividing the incorrect cost into actual investment distorts every utility's actual decision in a way that cannot be quantified. Dr. Overcast's approach to measuring TFP avoids this issue, since it treats each Company on its own and recognizes the different costs of capital by using an ex-post measure of capital costs.[346]

Implicit Assumption in Use of Indexes

211. A critical step in Dr. Lowry's methodology is, for each of labour and materials, to divide the nominal cost dollars by a price index to calculate a measure of inputs (the input quantity) in an index. For capital, the calculation involves two steps. First, the plant values are deflated by a construction cost index to establish a real value for the plant each year. That real value is then divided by a price index that is calculated as an industry average price of capital.

[345] Exhibit B-45, Overcast Rebuttal Evidence, p.29.

[346] Exhibit B-45, Overcast Rebuttal Evidence, pp.43-44.

This is reflected in the equations found at pages 76-77 (capital) of his Evidence.[347] Since the capital index deflator is the denominator, an index value larger than the actual change in the real price will yield a smaller real input value to be divided by the price index. Similarly, if the price index for labour represents a more costly basket of labour inputs than the utility actually uses, the resulting quantity of inputs is smaller than the actual inputs. If the overall input quantity measure is too small (which it is, for reasons discussed later), then the industry will appear more productive than it really is - i.e., it will have a higher TFP because it appears as though companies are using fewer inputs to generate outputs.[348] Given the nature of the formulae for calculating inputs, the input values for the industry are highly sensitive to the value of the price index and, in the case of capital, the capital index deflator.

212. Dr. Lowry used a single index for each cost (labour, materials and capital), adjusted only for regional differences. The index was not adjusted to reflect the actual mix of inputs for specific technology employed by the utility; thus, there is an implicit assumption that the companies in the sample to which the index is being applied are comparable in terms of the technology used, the mix of inputs and the mix of outputs.[349] If each utility has a different mix of inputs, the standardized measure of the input price index will not reflect the actual price of the inputs used to produce the total cost for a specific utility. Dr. Lowry acknowledged that this is an issue with his index choice but relied on the assumption that these individual errors will average out in the sample.[350] There is no averaging of errors when the index is too high under all circumstances. The index of input quantities is uniformly too low for every utility in Dr. Lowry's sample.[351]

213. While the assumption of uniform inputs may work well in the competitive environment, it will not hold true in practice for utilities. The input mix factor for either labour

---

[347] For capital, see equation [A8] in particular: FEI Exhibit C1-9-1, Errata to Lowry Evidence, p.77.

[348] Dr. Lowry confirmed this is the effect starting at T7:1421, l.20.

[349] Exhibit B-45, Overcast Rebuttal Evidence, p.4.

[350] T7:1395, ll.18-21 (Lowry).

[351] T7:1520, l.11-1527, l.25 (Overcast).

or capital differs from one utility to the next. Cost differences reflect those different mixes of inputs. Dr. Overcast explained:

> Simply dividing a price index into dollars [see equation above] does not produce a sensible or sound measure of the physical inputs actually used to serve customers. The net result is the competitive model assumptions do not apply and using an index across a utility sample does not properly recognize the differences in quality of inputs across utilities or the differences in technology sets employed by differing utilities. These input mix issues result directly from both environmental factors and from the differing sunk costs and regulated capital costs for utilities in different jurisdictions. Essentially, this means that the index methodology cannot be used across a sample of utilities because it cannot account for local operating environments or differing input mixes that result in the application of uniquely different technologies.[352]

214. Dr. Overcast expanded on this point in his Rebuttal Evidence:

> The technology set assumption issue in PEG's testimony is significant. To begin it is necessary to explain the significance of the production technology set. While in theory this concept is explained elegantly using set theoretic notation, it is simply a statement that a multi-output production technology can be defined by the combination of inputs used to produce those outputs and the output actually produced is part of the technology set. This is important for measuring productivity over time as technology changes there is a different technology set each year. PEG's index numbers rely on the assumption that this technology set is the same for each utility in the sample in any given year and that all utilities are measured against that technology set as discussed above related to index and price measures. The reason that this assumption is required is because they use a standardized index to measure real cost based on a specific set of inputs. Utilities with differing technology sets will use different inputs (the input mix) that would result in a point on a different cost curve that cannot be used to determine either the real cost of capital additions or the price of capital because of different expected lives of assets based on the type of asset. The PEG assumption is correct if the analysis was for a competitive market because capital moves freely and technology is not a barrier to entry. The implicit assumption in PEG's analysis is that capital is freely disposable and may be replaced each year. In the world of utility regulation it is precisely the absence of

[352] Exhibit B-45, Overcast Rebuttal Evidence, p.30.

> these competitive market features that leads to regulation even though PEG relies on the competitive paradigm for the basis of its analysis.[353]

215. Dr. Overcast then provided further explanation, and a number of real world examples of why the assumption that utilities have the same technology set (as they would under the competitive market paradigm) is not valid in the context of regulated utilities with sunk costs, lumpy capital additions, administratively determined cost of capital, and certain operating conditions.[354] He offered the following analogy for why the indexed based approach does not yield useable results for utilities:

> PEG has compared apples to grapes and cherries and so forth with no reasonable basis for creating a basic index number since each utility has different inputs, outputs, input prices, technology, weighting factors for inputs and outputs all resulting in a meaningless index. This would be like calculating the CPI using different market baskets and different weights for each type of good and proclaiming that the result reflects the change in consumer prices for all consumers.[355]

216. The problem of measurement error plays out in Dr. Lowry's determination of the labour cost inputs. Using an index to deflate labour costs requires assuming all utilities use the same market basket of labour inputs so that when the price index is divided into costs the resulting quantity index is the actual quantity used by each utility. For this assumption to be true, it is necessary to assume that the utilities are using the same basic technologies and production processes. Further, it is necessary to assume that the general index being used is also representative of the actual types of labour employed. This is not a problem for competitive industries because all firms use the same technologies and mix of labour types as they move to long-run equilibrium.[356] The assumption does not hold true for utilities, and the differences among utilities aren't captured.[357] Dr. Overcast explained:

---

[353] Exhibit B-45, Overcast Rebuttal Evidence, p.38.

[354] Exhibit B-45, Overcast Rebuttal Evidence, pp.38-39.

[355] Exhibit B-45, Overcast Rebuttal Evidence, p.39.

[356] Exhibit B-45, Overcast Rebuttal Evidence, p.12.

[357] Exhibit B-45, Overcast Rebuttal Evidence, p.11.

> If gas main maintenance requires a significant amount of hand labor to uncover the main (as would be the case in an urban setting) the mix of labor inputs would differ from the case where the main can be uncovered by a piece of capital equipment with a skilled operator. The PEG price index that is critical to PEG's determination of the input quantity for labor cannot distinguish between labor types that have different costs and hence different weightings in the proper price index used to calculate the inputs. Under the PEG method for estimating labor inputs, two utilities in the same region with identical labor costs would have identical labor inputs under the PEG assumptions.
>
> There is so little difference in the PEG labor cost index over the sample period that one is led to believe that the labor inputs are all assuming the same basic technologies and production processes for all utilities as well. In reality, two utilities could have the same labor costs and different levels of labor input because they use a different mix of labor and capital in different parts of the business. Theory is unambiguous that both the quality and the quantity of labor matters. This is a logical conclusion since in a competitive labor market the payment to labor matches the marginal productivity of the labor input. In our example above the skilled operator of a backhoe earns more per hour that the man with a shovel. For example, an urban utility may have more service personnel because of the need to excavate main by hand but reads meters remotely or has out sourced meter reading while another utility may read meters but use capital equipment to excavate mains. The net result is a different number of employees with different skill levels and different prices that cannot be reflected in the PEG analysis. Thus a measure of the quantity of labor under the PEG method for comparing the two utilities has no relevance.

217. Dr. Overcast cited several examples to demonstrate how labour costs differ from utility to utility. For instance:[358]

> Consider the cost category under distribution operations defined by the uniform system of accounts Account No. 871 - Distribution Load Dispatching. This account represents the people who operate the system on a daily basis. This requirement may be outsourced to a third party, provided by a supplier or provided internally based on a variety of factors. The activities of these individuals differ from utility to utility as the result of a number of different supply alternatives and the type and number of different supply options available for the utility. Their work is complicated by the number of city gates, available primary and secondary delivery points for supplies, the number of pipeline suppliers, the services available from each supplier, the number and

[358] Exhibit B-45, Overcast Rebuttal Evidence, pp.11-12.

> type of storage services under contract and the availability of peaking supplies such as LNG.

218. Dr. Lowry's index for materials, rents and supplies and labour suffers from similar issues:

> The index that PEG uses is a weighted value that reflects both labor prices (with the problems noted above) and an index designed to reflect materials, rents and supplies. PEG has filed no evidence related to the index as it is a proprietary service. Nevertheless, having done a significant number of cost of service studies, I am familiar with the residual accounts that make up the materials, rents and supplies and these include a variety of accounts that have multiple components. For example, the account outside services includes any number of utility activities that differ from one utility to the next. It would be unreasonable to think that a single index could adequately address the various combinations of activities recorded in this account. Thus it is likely that the measure of inputs results in inconsistent measures for the same reasons that apply to the other price indices discussed above. That is the index used for converting dollars of costs to units of inputs cannot possibly reflect the differences that are included in these accounts for each utility. If the index cannot properly measure inputs as in this case there is no basis for concluding that the TFP estimate is reliable.[359]

219. Similar issues exist with capital. Dr. Lowry's approach to capital inputs assumes that a regional index of construction prices (the Handy-Whitman Index) is adequate for adjusting the nominal dollars of capital to real dollars. Dr. Overcast explained that for this assumption to hold true, all utilities would need to use the same production technology set just like competitive firms that all use the same inputs to produce outputs.[360] Dr. Overcast explained that, in the context of utilities, "The use of any standard index would obviously not reflect the mix of inputs used for any one utility from year to year and could not possibly reflect a comparison of costs across utilities as noted by the authors of the Handy Whitman Index".[361] He provided several examples to illustrate the likelihood that this assumption will introduce measurement error in determining capital inputs:

---

[359] Exhibit B-45, Overcast Rebuttal Evidence, pp.49-50.

[360] Exhibit B-45, Overcast Rebuttal Evidence, pp.29-30.

[361] Exhibit B-45, Overcast Rebuttal Evidence, p.13.

> Gas utilities use both steel and plastic main depending on a number of factors. While the size of the main may be the same, 2 inch pipe for example, each type of pipe and size has a different cost so each utility could have the same total cost but purchase different quantities of inputs. This difference would not show up in the PEG analysis of the real value of the plant investment leading to an incorrect measure of the capital inputs assuming that the price of capital is correctly estimated. Further, the capacity value of steel pipe differs from plastic because steel pipe can operate at higher pressures and thus adds more potential capacity to the system than a comparable size of plastic pipe.
>
> ….
>
> [U]tilities all use different technologies to produce outputs unique to their service area. The differences in technology result from a number of local factors that influence the cost of identical physical facilities being installed even within the same utility. Black & Veatch has filed evidence in cost of service filings that costs differ between suburban and urban main installation based on a variety of factors. It is also true for electric utilities that use different construction methods for transmission and distribution facilities based on the environmental factors such as requirements for undergrounding facilities in some areas (a factor that PEG recognizes). Further, some utilities use "tree wire" or other coated wire in areas with more trees to minimize outages or faults and reduce maintenance costs. This technology costs more that standard wires. The PEG methodology would measure this as more physical inputs not as a different quality of input based on a different technology.
>
> The same might be said for electric utility costs where utility pole technology encompasses poles of different costs made from wood, concrete, steel, composite materials, etc. In addition, the size of poles (measured in both length and class) causes cost to be different and there is no one set of standardized pole length or class for each utility. A number of factors impact the length and class of pole installed. As a simple example, mounting a 50 kVa transformer on a utility pole typically requires not only a longer pole but a heavier class of pole thus a more costly pole. The mix of pole types effects costs and thus would show up as input differences not as quality and technology differences.

220. Dr. Overcast concluded: "The fundamental point is that higher costs for one utility compared to lower cost for another does not mean that the second utility uses less inputs just that the inputs are included elsewhere and amounts to a measurement error under

the PEG method."[362] Individual errors in measurement can add up to large errors in the measurement of TFP when using an index-based method.

221. Dr. Overcast recognized that it is not possible to develop an exact measure of TFP, but in his original TFP Reports had stressed the importance of trying to make assumptions as realistic as possible: "Using measures of inputs and outputs that are not rooted in the reality of the utility operation produces misleading results and can cause a TFP that is unfair to either the customers or the utility."[363] Dr. Overcast elected to derive a central tendency based on actual utility-specific data in part to avoid the need to make the assumption implicit in traditional index-based methodologies that utilities in the industry will have uniform production sets.[364] His approach resolves the issue of sunk costs and the impact on technology choices because the utility knows its own options and invests in technology as those own costs and prices justify.[365] Measurement error of the type implicit in the use of indexes is limited under Dr. Overcast's approach to the much narrower circumstance where a particular utility has switched from one production method to another during the sample period.[366]

Dr. Lowry's Choice of Labour, Materials, Rents and Supplies Index Biases TFP Upwards

222. In order to measure the inputs associated with O&M and Administration & General expenses, Dr. Lowry used as his deflator a weighted value that reflects both labour prices and an index designed to reflect materials, rents and supplies. Dr. Overcast identified potential upward bias with both.

---

[362] Exhibit B-45, Overcast Rebuttal Evidence, pp.11-12.

[363] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), pp.2, 6. Dr. Overcast also later noted in his Rebuttal Evidence, "It is far more difficult to model reality than it is to assume away the messy problems and produce a stylized version of TFP that is not reflective of anything other than the assumptions that abstract from the reality." Exhibit B-45, Overcast Rebuttal Evidence, p.13.

[364] Exhibit B-45, Overcast Rebuttal Evidence, p.8.

[365] Exhibit B-45, Overcast Rebuttal Evidence, p.42.

[366] Exhibit B-45, Overcast Rebuttal Evidence, pp.11-12.

223. With respect to Dr. Lowry's use of the Employment Cost Index ("ECI") as the price of labour for determining the labour input, Dr. Overcast provided several reasons why it understates the price of labour incurred by utilities:[367]

- First, the index only represents the salaries and wages of the labour force, which (based on data from the Bureau of Labor Statistics wages and salaries) represents only about 70 percent of the total compensation for utility employees. Dr. Overcast explained that "When analyzing the economics of capital and labour substitution, utilities use the total compensation of labour. More importantly, the total compensation of labour is the value used by utilities to make decisions relative to efficient production of outputs." [368]

- Second, the salary and wage index is not based on the total employment for a utility but only a segment that includes craft employees and the first line of supervision. In other words, it does not account for employees that work and support the craft employees. The inclusion of lower paid support employees would have lowered the index value, and their exclusion biases TFP upwards.[369]

- Third, the ECI includes representative of highly skilled labour cohorts such as generation plant operators, including the operation of nuclear power plants. Nuclear technicians and plant operators are obviously highly skilled, and hence costly, labour. Their inclusion increases the index value (biasing TFP upwards).[370] Dr. Overcast elaborated on this particular point under cross-examination:

---

[367] Exhibit B-45, Overcast Rebuttal Evidence, pp.48-49.

[368] Exhibit B-45, Overcast Rebuttal Evidence, pp.48-49.

[369] Exhibit B-45, Overcast Rebuttal Evidence, pp.48-49. Dr. Overcast quoted the official definition of utilities from the Bureau of Labor Statistics: "The Utilities sector comprises establishments engaged in the provision of the following utility services: electric power, natural gas, steam supply, water supply, and sewage removal. Within this sector, the specific activities associated with the utility services provided vary by utility: electric power includes generation, transmission, and distribution; natural gas includes distribution; steam supply includes provision and/or distribution; water supply includes treatment and distribution; and sewage removal includes collection, treatment, and disposal of waste through sewer systems and sewage treatment facilities."

[370] Exhibit B-45, Overcast Rebuttal Evidence, pp.48-49. Dr. Overcast quoted the official definition of utilities from the Bureau of Labor Statistics.

> Now, I can't test the whole O&M component *[Note: the index that Dr. Lowry used for materials etc. are proprietary and were not disclosed]* but I can test the part of it where he divides the dollars of payroll by a price to get a quantity of input, and the price he uses is a report from the Bureau of Labour Statistics, and if you go and look at that report and you say, "What makes up this price?" the highest hourly rate in that index is for nuclear plant operators.
>
> Now, I'm reasonably certain that Fortis Gas doesn't have any nuclear power plant operators. And I'm also pretty certain that B.C., or that FortisBC doesn't have any either. That was the highest paid.
>
> The second highest paid set of employees in that study were power plant operators. Again, Fortis Gas doesn't have any of those either. And so what he's done is, he's taken an index that is too high to divide into dollars to get the input units associated with labour. That again biases the TFP to be too high. And the net result of all that is that his input indexes are all wrong.[371]

224. In summary, the partial factor labour productivity in both gas and electric industries during the period 2002 through 2011 is only a small positive value based on data from the Bureau of Labor Statistics employed by Dr. Lowry.[372] This value exhibits upward bias. As discussed below, Dr. Lowry's capital measure is, by far, the greatest contributor to his large positive TFP for the gas and electric utility industries. The issues with Dr. Lowry's determination of capital inputs, discussed next, are far more pronounced.

Dr. Lowry's Calculation of Capital Inputs Subject to Upward Bias

225. Dr. Lowry's calculation of capital inputs significantly understates the capital inputs used by the electric and gas industries (i.e., makes them look more productive than they really are). The upward bias is related to both:

- the omission of material capital costs from the nominal values by virtue of his use of linear depreciation and exclusion of net negative salvage; and

[371] T3:462, l.19-463, l.13 (Overcast).

[372] Exhibit B-45, Overcast Rebuttal Evidence, p.49.

- the fixed-weight index deflator - the Handy Whitman Index - that significantly overstates capital cost inflation for utilities.

Since capital forms the vast majority of the overall inputs for an electric or gas utility, Dr. Lowry's measured TFP's for these industries are much too high.

Nominal Value of Capital Understated Due to Service Life Assumptions

226. The nominal value of inputs is the numerator in Dr. Lowry's capital input calculation, which is then divided by the Handy-Whitman Index to yield real dollars. If the nominal value (numerator) is too small, then under Dr. Lowry's formula the resulting capital input value will be too small.[373] TFP will be too high. Dr. Lowry made a number of assumptions that had the effect of excluding nominal costs from consideration, the most notable of which was his use of uniform linear depreciation to represent declining service value of capital inputs for all utilities.

227. Dr. Lowry explicitly assumed that the service value of capital inputs declines on a straight-line accounting basis, and that capital inputs provide no service value after being fully depreciated. In the case of the gas industry, assets over 41 years were assumed to have no service value for producing outputs.[374] For electric utilities, Dr. Lowry assumed 44 for distribution and 16 years for general plant.

228. Dr. Overcast explained why explicitly assuming uniform depreciation among all utilities in the sample is a significant abstraction that will lead to measurement error:

> There are a number of reasons that such an assumption is incorrect. First, if asset lives were the same as stated in the PEG report, there would be no need for individual utilities to conduct depreciation studies to support the level of

[373] T7:1433, l.23-1434, l.22 (Lowry).

[374] Exhibit C1-9, Lowry Evidence, pp.76-79. Under this calculation, Dr. Lowry assumes that the measure of input deteriorates at the rate of 100% divided by the value of the average life of the asset. Using the 41 year life assumed by Dr. Lowry, the service flow value of an asset declines by about 2.44% per year and there is no service flow value for an asset older than 41 years. That is, if a gas LDC has pipe older than 41 years, the input value of that pipe is assumed to be zero for purposes of the input index used in the report.

> depreciation expense in their revenue requirements. Second, environmental factors influence the expected life of utility assets and those factors vary from utility to utility and even within the same utility. Third, the different mix of assets used by each utility (the percentage of total pipe that is plastic pipe) differs for many reasons such as historic growth rates, location of pipes on the system and so forth. This means that each utility has a different composite asset life. Using a single measure of depreciation life for purposes of measuring the price of capital is not a valid assumption and results in an incorrect indirect measure of physical capital inputs for each utility in the sample. [375]

229. Since it is self-evident that Dr. Lowry's assumption will inevitably result in measurement error, the only questions are the extent of the measurement error and whether the error presents a systematic bias. Dr. Overcast characterized Dr. Lowry's service value assumption as "a material error that invalidates the results of the PEG study both theoretically and practically. As with other parts of the capital value estimate, this causes TFP to be overstated and this is a consistent bias in the PEG report."[376] The evidence on the record demonstrates that Dr. Lowry's approach of assuming that service life declines on a straight-line basis introduces a systematic upward bias on TFP:[377]

- ***Operational reality is that assets continue to have full service value:*** Dr. Overcast's critique aligns with operational reality for electric and gas utility plant. He used the example of gas plant to illustrate his point, but emphasized that the same considerations apply to the electric industry:

  > It is important to recognize a distinction between the capital in mains, meters and services as compared to the traditional views of capital. Under the traditional view of capital, depreciation measures the decline in productivity from using an asset over time. For the bulk of gas distribution and transmission, the productive capacity does not change over time. That is, the capacity of a segment of pipe remains the same over its life. In fact, based on the rating of the pipe segment, the actual capacity may be increased just by raising the operating pressure on the pipe. Raising operating pressure is possible so long as the current

[375] Exhibit B-45, Overcast Rebuttal Evidence, p.28.

[376] Exhibit B-45, Overcast Rebuttal Evidence, p.29.

[377] Exhibit B-45, Overcast Rebuttal Evidence, pp.21-24.

> operating pressure is less than the maximum allowable operating pressure of the pipe. This would allow for added throughput with no additional investment.[378]

And further:

> PEG simply makes an assumption that can only produce a positive value of TFP because it fails to recognize that infrastructure has the same type of depreciation as a structure. The service value of the infrastructure is unchanged by age so long as the facilities are maintained in good working order. To illustrate the reasonableness of this conclusion, the following table provides a listing of the factors that impact the flow of gas through the pipeline system under the IGT Distribution Equation. This equation is used by gas planning engineers to determine the size of pipe required to serve load while maintaining minimum system pressures under design day conditions to provide reliable service. It represents the method for calculating the change in system capacity from the addition of pipe miles by size and operating pressure.
>
> [Table 1 omitted]
>
> This equation contains no term that relates to the age of the pipe. With the exception of the term Pipeline Efficiency, all terms are determined exogenously. Pipeline efficiency relates to the inside of the pipe relative to the smoothness factor resulting from the manufacture of the line. That term does not change over time since a well maintained line has no internal changes as the result of gas delivery.
>
> Further, there is ample empirical evidence that physical assets such as pipelines do not deteriorate as hypothesized by PEG because the design day requirement of a gas LDC is met making use of assets that for book purposes are fully depreciated. This conclusion holds for the entire LDC population of the United States where over 39 percent of all gas main in service in 2011 is older than 41 years. The same is true for electric assets as well although it is somewhat harder to measure because electric utilities do not report this age information like gas LDCs provide

[378] FEI Exhibit B-1-1, FEI Application, Appendix D2, Estimating Total Factor Productivity (Erratum Exhibit B-1-4), pp.3-4.

> annually. The result of this incorrect measure of capital inputs results in an upward bias in the academic estimate of TFP and causes the recommended X-Factor provided by the PEG testimony to be meaningless.[379]

FEI included as part of its Long-term Sustainment Plan a discussion about the fact that asset age does not dictate the timing of replacement. FEI concluded that assets can remain in service for many years beyond the depreciable life.[380] A third of FBC's transmission lines are older than the 44 year service life assumed by Dr. Lowry.[381]

- ***Assumption that service value matches accounting depreciation has asymmetrical impact (upward bias):*** The upward bias inherent in an assumption that assets have no service value after being fully depreciated for accounting purposes is not counteracted by the fact that some assets are taken out of service before they are fully depreciated. Ms. Roy and Dr. Overcast explained that so long as an asset is in use still, it stays "on the books". By contrast, when an asset is retired early, "we actually go to the process of removing the asset from our books, it doesn't exist there anymore at all". Since the retired asset is removed from the books, there is no potential for that asset to cause the service value of assets (nominal inputs) to be overstated.[382]

- ***Illogical result:*** Dr. Overcast observed how Dr. Lowry's assumption of straight line deterioration of capital service value contributes (along with a mis-specification of outputs by excluding a capacity measure) to the illogical result of utilities in Dr. Lowry's sample showing input declines and increases in output to the extent where the level of inputs could not physically meet the firm design day requirements of the utility:

---

[379] Exhibit B-45, Overcast Rebuttal Evidence, pp.22-23. See also: T7:1509, l.2-1510, l.9 (Overcast).

[380] FEI Exhibit B-1-1, FEI Application, Appendix C3, p.2; FEI Exhibit B-24, BCUC-FEI IR 2.340.1.

[381] T7:1507, ll.8-25 (Overcast).

[382] T3:484, l.13-486, l.10 (Overcast, Roy).

> The correct specification for input quantity does not include the deterioration of capital as PEG has done. Since the capital inputs are critical to produce current outputs, regardless of the year of installation, PEG uses an inappropriate measure of capital input that significantly understates the actual changes in that input as discussed above. In fact, PEG shows low or declining capital inputs for half of the years in their sample despite the persistent growth in both capacity and customers across the sampled data. This is actually a physical impossibility since gas LDCs could not meet the design day requirements of customers under these conditions.
>
> A similar result appears for electric utilities with negative growth in capital inputs in the later years and extremely low growth in inputs in the earlier years despite robust growth in outputs. Since all new customers require new capacity, it is not surprising to see persistent growth in capacity as measured by substations over the period. This same point illustrates the fundamental failure of the PEG study to measure the output mix of customers and capacity. Simply using customers only is a fatal flaw because the change in the number of customers without the measure of capacity does not properly recognize the difference in infill and system expansion customer mix. By adding a capacity measure both elements of the mix are included in the output. The PEG study does not recognize or account for this difference and thus the residual measure of TFP is incorrect. These errors lead to TFP estimates much higher than the actual TFP results that would occur if the capital input is measured properly. [Emphasis added][383]

230. Since the TFP measure calculated by Dr. Lowry cannot physically meet the firm design day requirements of customers, the changes in input cannot match the change in output in any physical sense. This artificially raises the TFP value by showing a smaller change in actual input than really occurs.[384]

[383] Exhibit B-45, Overcast Rebuttal Evidence, pp.27-28.

[384] Exhibit B-45, Overcast Rebuttal Evidence, pp.21-22.

231. Dr. Overcast elaborated at the hearing as to why Dr. Lowry's method of determining service value of capital assets, while theoretically acceptable, produces results that are incorrect for utilities in practice:

> Dr. Lowry's method is theoretically an acceptable method, but practically it's incorrect. It's incorrect because he underestimates the number of input units associated with capital by the way he makes the calculation. And I can prove that mathematically, if you would like. I'll step up here to the board and give you all the equations and show you how he underestimates it.
>
> But he underestimates it because he assumes that the service value of an asset declines at the same rate as it's being depreciated for rate-making purposes, and that's factually incorrect. There are pipes in the ground in gas LDCs here and elsewhere that are way over 41 years old, and they're still providing the same service value. He assumes that any pipe that's older than 41 years has no service value. And in effect, he's in the position of saying output grew, and the inputs required to produce that output are actually less than the inputs that you could produce that output with. Because he's thrown out this pipe that is actually used to provide that service. He's just simply eliminated from the analysis.
>
> And so when you go through that, and you know that there is pipe in the ground that's providing full service, the same service it provided when it was new, that's still an input, and that input has to be counted. Otherwise, you're underestimating the number of input units.[385]

In light of the engineering and operational realities of utility plant outlined above, a better assumption would have been to assume that an asset retains its service value until taken out of service (as would be reflected in the "one-hoss shay" depreciation method).

232. Dr. Lowry, in his opening statement/sur-rebuttal, quoted a 2004 paper from Dr. Deiwert (a well-known scholar at UBC) in which the author had suggested that it is not appropriate to use the one hoss-shay method of depreciation. This is a demonstration of Dr. Lowry not being up to date on the literature. Dr. Overcast pointed out that Dr. Deiwert had subsequently changed his view in that regard. Dr. Deiwert is now critical of the approach taken by Dr. Lowry, for the very same reasons that Dr. Overcast had discussed. Dr. Overcast stated:

---

[385] T3:458, l.12-459, l.14 (Overcast).

> And I will actually give you an example I read this morning earlier that in his sort of call it rebuttal to my rebuttal, sur-rebuttal, whatever, he cited a professor who is at the University of British Columbia here as a source for saying that you couldn't use one haul shay [sic- one hoss shay] depreciation. And that paper was written in I believe 2004, 2005, according to the footnote, but that is the exact same professor who authored a study four years later who says that Dr. Lowry is wrong for not using one haul shape [sic- one hoss shay] depreciation. And what has happened is, as academics understand more and more about the business, they have learned more and more about how to make these studies more realistic, and you know, the academics are only as good as what they really understand about the practical reality of the gas business. And the practical reality, which is where my strength is -- I mean, I am no great theoretician or anything like that, I mean I am not going to go out and be some great theoretical person. My strength is being able to apply economics to the real world, and I understand the real world constraints, and that real world constraint is, in the case of, in the case of capital, there is no diminution of the service value of a well maintained asset over its life.
>
> And it's not just me saying that. I mean academics who understand are saying that, and on top of that I believe that -- and I can ask Ms. Roy to comment, but I believe there's actually a report from Fortis that says the exact same thing because they figured out that it really isn't the age of the asset that affects its service value. Even if it's fully depreciated it still has service value if it's well maintained. …[386]

233. The result of Dr. Lowry's depreciation assumption is that inputs are significantly understated for the electric and gas industries, and thus TFP is significantly overstated. Dr. Overcast's methodology accounts for all of the pipe in the capacity output and reflects the impact on costs in the use of net plant as a measure of capital input.[387]

Assumption of No Net Salvage

234. Dr. Lowry's nominal input costs for each utility in his sample (numerator) also do not account for net salvage. Net salvage may be either positive or negative depending on the asset class. For example for vehicles the net salvage would likely be positive, while for assets that have a cost of removal and only scrap value net salvage would likely be negative. Pipe

[386] T3:468, l.3-469, l.11 (Overcast). See also: T7:1505, ll.4-22 (Overcast).

[387] Exhibit B-45, Overcast Rebuttal Evidence, p.28.

represents the single largest component of gas distribution and transmission plant, and its net salvage value will generally be negative because of the cost of removal. The same is true for electric distribution and transmission plant. As with other parts of the capital value estimate, Dr. Lowry's omission of net salvage from the input calculation caused his input quantities to be understated and his measured TFP for the gas and electric industries to be overstated.[388]

Using the Handy-Whitman Index as a Capital Deflator

235. Dr. Lowry's TFP calculations for electric and gas are heavily influenced by the deflator that he uses for adjusting the nominal dollars of capital to real dollars. If the deflator is wrong, then the result is an inappropriate input quantity measure even if all other factors in the input analysis were correct. There are two reasons, discussed below, why Dr. Lowry's choice of the Handy-Whitman Index as his deflator to deflate nominal capital cost values into real dollars introduced significant upward bias in his TFP calculations.

236. First, the Handy-Whitman Index is a fixed base index using 1973 as the base, which means the index weights are frozen in time as they existed 41 years ago. Dr. Lowry's selection of a fixed-weight index with a distant base year is at odds with the views of Coelli, et al., in their text on efficiency and productivity, who emphasize that indexes used in the context of productivity studies should be chain-weighted (not fixed) so that the weights in the "basket" change to keep pace with developments over time. Coelli, et al. state:

> If you are working with a long time series data, it is appropriate that you make use of a chain index. In any case it is important not to use an index that makes use of a base period which is too far from the current period.[389]

Dr. Lowry's use of a fixed-weight index with a base year over 40 years ago has significant ramifications in this case:

---

[388] Exhibit B-45, Overcast Rebuttal Evidence, pp.28-29.

[389] Exhibit B-45, Overcast Rebuttal Evidence, p.24.

- In 1973, utilities used a very different mix of materials than is used today. For gas utilities, the cost of pipe is by far the largest capital cost. The mix of installed pipe has shifted from mostly steel in 1973 to mostly plastic in 2011. The cost of plastic pipe has increased a lot slower than steel pipe, which can be seen from looking at the 2011 Handy-Whitman Index values for steel main and plastic main in Confidential Exhibit B2-31. By 2011, the cost of steel pipe had increased by 257 basis points MORE than the cost of plastic pipe - a very significant difference. Since the Handy-Whitman Index still assumes that utilities are installing primarily steel pipe as they were in 1973, the index deflator that Dr. Lowry used was very significantly overstated throughout Dr. Lowry's study period. Dr. Lowry's use of a denominator in the input formula that is overstated to the extent of 257 basis points by 2011 significantly understates inputs for the gas industry and yields an excessively high TFP.[390] Dr. Overcast addressed this point in his Rebuttal Evidence:

> The Handy Whitman Index also provides sub-indexes for different types of main installed. Table 3 below illustrates the differences in the cost for steel and plastic main in the period used by PEG. It is easily seen that different input mixes would result in a different composite index for each utility and this invalidates the use of a single index for each utility in a region as the basis for determining the real value of the costs incurred. If that value is wrong, the input quantity is wrong as the result of measurement error.
>
> …
>
> Table 3 provides evidence that the changing pattern of cost for steel and plastic main is dramatically different over the PEG study period. Main is the single largest category of capital for gas LDCs and typically represents between 40 and 50 percent of distribution gross plant. Further, steel and plastic are also the most typical types of service lines. Including service lines with main would, in total, result in about 70 to 80 percent of distribution gross plant. The magnitude of the impact on the

[390] T7:1432, l.8-1433, l.5 (Lowry).

> input measure of capital from assuming a single value for determining the real cost of plant would be quite large during this period.[391]

Dr. Overcast elaborated under cross-examination:

> There is also an error that he makes in the analysis because in his process, he calculates the real value of capital. And that real value of capital is a function of the incremental capital investment in one year, adjusted by the Handy Whitman index, and he uses the total for gas, for example, he uses the total Handy Whitman index for gas construction.
>
> And that index is a fixed base index. It's based on 1973. And in 1973, you can look at the pipeline and hazardous materials safety administration and find out that in 1973 if you take all the companies in the U.S. that steel accounted – steel main accounted for 93 percent of main, and plastic main accounted for 7 percent of all the main at that time. And so, if you assume that there -- which is proper, if their weights were fixed in that period, they would be heavily weighted towards steel. If you look at the Handy Whitman index, you can confirm that that's true, because the Handy Whitman index is substantially higher than the cost of plastic main, and only slightly lower than the escalation rate in steel main.
>
> A main makes up 50 percent, roughly 50 percent of the capital costs. If you add services and the same thing is true about services, steel is more than plastic, that makes up another 20 or 30 percent, so you're already at the 80 percent of the cost of capital -- or 80 percent of the value of the capital.
>
> And when you look at the modern era, plastic began to be installed in the sixties. In 2011, for that year, the average for the U.S. based on the pipeline and hazardous safety material administration reports that are required by federal law in the U.S. says that the weights are 15 percent for steel and 85 percent for plastic. And now the Handy Whitman Index actually splits out plastic and steel so you can get the relative cost differences. And

[391] Exhibit B-45, Overcast Rebuttal Evidence, pp.26-27.

let's see, I think I can tell you the number for the Handy Whitman Index on steel and plastic.

Now, remember the index is fixed base, so in 1973 steel and plastic were both at 100, okay? That's what a fixed base index is. It's like the CPI. You'll see a thing that says CPI. 1983 equals 100, whatever the year is. So both plastic and steel were at 100 in 1973. In 2011 steel was at 776 and plastic was at 519. So that means steel had increased by roughly 257 basis points faster over that period than the plastic pie.

The overall composite index for the Handy Whitman in 2011 was 722. You can see that's substantially higher than the 519 for plastic pipe. Okay? And so now remember I told you that 85 percent of the pipe was plastic, and if you just took and weighted those two components for plastic and steel, the right number to divide by for main, instead of being 722 would be 557. And what that does is when he deflates the nominal value into current – into constant dollars, he is using too big a number to divide into. So he's getting too much smaller a real value of plan[t]. Those are all facts. He's getting the number that results in lower cost.

Now, what he does is he takes the equation price times quantity equals total cost in real terms. So if the total cost number is too low and he divides by a price factor, then he's going to get too few quantity inputs. And unfortunately, all throughout his study what he's done is he has calculated too few inputs. And if inputs are smaller than they're supposed to be, the formula is quantity -- I mean is TFP equals output minus input. And so if the input is too small then you're going to have TFP being too large for a given set of outputs. And that's where he's fallen apart here with his analysis.

Literally he not only has this error but he compounds it by saying that this pipe that I've put in, in 1980 or 1990, doesn't have the same capacity today. So he's discounted it again. And that means that he has used way too low an input number, and when you do that you get way too high a TFP.[392]

[392] T3:459, l.15-462, l.18 (Overcast); see also T7:1520, l.21-1523, l.1 (Overcast).

Similar issues exist for the electric industry. Dr. Overcast explained how, since 1973, copper conductor has been replaced by much cheaper aluminum conductor. Copper conductor is now basically used only for ground wires. In the fixed-weight Handy-Whitman Index, copper has a much higher weight and a much higher cost, which means that the deflator is too high, yields inputs that are too low, and a TFP for the electric industry that is too high.[393]

- Second, the Handy-Whitman Index does not reflect any technological change that has occurred since the base year 1973 -- a point that the authors of the Handy-Whitman Index are careful to note. This amplifies the upward bias discussed above because the Handy-Whitman Index does not account for cost savings that are attributable to technological change. The value of the index is too high when compared to today's construction costs. Under Dr. Lowry's methodology, when the deflator (denominator in the input formula) is too large it produces lower capital inputs. Lower inputs mean higher TFP. This affects both the gas and electric industries:

    - Since 1973, there have been major changes in the technology for installing and replacing mains including live insertion and directional drilling.

    - Electric utilities have reduced the amount of secondary delivery systems that they use, and increased the primary systems. They have also increased the voltages of the primary services. The result is that the costs will be higher, but the output capability increases more than the cost increase. So the per-unit cost of capacity, because of scale economies, is lower. Dr. Overcast explained that this "results in an under-estimation of input units, and it also means that if you don't have

[393] T7:1512, l.3-1513, l.11 (Overcast).

> capacity in there as a measure, you're not going to pick up the effect of those economies of scale."[394]

This is the same substitution bias that Dr. Lowry recognizes with respect to CPI in arguing that that this bias overstates CPI by 50 basis points per year, a much smaller amount.[395]

237. Dr. Lowry conceded that there is "probably a little bit of overstatement of inflation in our indexes because the sub-indexes have fixed weights".[396] The evidence presented by Dr. Overcast demonstrates that the extent of the "overstatement of inflation" is significantly more than just "a little bit".

Dr. Lowry's Capital Formula Produces Strange Results

238. Dr. Overcast observed that Dr. Lowry's overall approach to calculating capital inputs produced some counter-intuitive results, which do not arise when Dr. Overcast's direct measurement approach is used:

> In reviewing the PEG calculation of the change in inputs over this period PEG reports that on 371 occasions the quantity of capital inputs declined out of 832 observations or on 44.6% of all observations the change in the capital input was negative. This result follows from the cumulative impact of an improper deflator and an erroneous calculation of the capital price as discussed above. This would imply automatically that TFP would be positive for those observations since the formula is TFP equals a change in output minus a change in input. The subtraction of a negative value means adding to the TFP.
>
> It is relatively easy to test this result by reviewing either the physical miles of main additions or the gross capital investment. Using the PEG raw data from the report, the actual capital investment is positive in all but 92 periods. This means that even on a real basis capital inputs actually increased. More importantly, if

---

[394] T7:1513, l.12-1516, l.7 (Overcast).

[395] T7:1393, ll.11-17 (Lowry). Substitution bias means that when the index is used to convert nominal dollars to real dollars the estimate of real dollars is too low. The CPI example is not applicable in the context of the TFP since it is not used as a price in any of the analysis. It is used here to show that the very concern expressed by Dr. Lowry as it relates to using CPI as part of the measure of inflation wasn't accounted for in his own analysis.

[396] T7:1396, l.24-1397, l.9 (Lowry).

> one looks at the actual dollars expended those are positive for every utility in the sample for 2007 through 2011, the period for which B&V had collected the data on mains and services when PEG shows negative change in investment in real terms for 29 times.
>
> This is in contrast with the B&V results which use the growth in net plant to measure capital inputs and avoids the issue of large or significant numbers of negative changes in the capital input measure. Further, the B&V approach uses a single measure of all inputs that reflect every element of capital costs including negative salvage and positive salvage, and all of the O&M costs in one total input amount and compares that only in the context of the same set of factors reflected by each utility in the sample. This means only assuming the conditions for each utility reflect its own change in input and output mix and in the technology set. This is the only theoretically valid assumption for all the reasons discussed above.[397]

Adjusting for Input Errors Alone Leads to Negative TFP

239. Dr. Overcast was confident that - wholly apart from the upward bias associated with Dr. Lowry's choice of output measures - correcting the input measure alone for the issues discussed above would yield a negative TFP value:

> And I also disagree with him on the output index, but for our purposes at this point I've just demonstrated from factual evidence that you can verify readily that his TFP estimate is too high. <u>And I'm confident that if you adjusted these for the right levels of inputs, the number would be negative</u>. And so my number is negative. It passes the test of -- people are investing in new plant and equipment associated with infrastructure replacement, which doesn't change the output. And so if output is constant, the inputs are going up, because of that, TFP has to be negative. It's that simple. [Emphasis added.][398]

(e) Dr. Lowry's Decision Not to Calibrate X-Factor As He Has Done in Other Cases

240. Dr. Lowry departed from the theoretical logic of his own approach, and his past testimony, by recommending the use of the macro-economic inflation measure BC-GDPIPIFDD for the I-Factor without "calibrating" the X-Factor to ensure that the PBR formula is reflective of

---

[397] Exhibit B-45, Overcast Rebuttal Evidence, p.31. The cross-examination of Dr. Lowry on this point, using Exhibit B2-32 excel spreadsheet, begins at T7:1438, l.14 (Lowry).

[398] T3:463, ll.14-25 (Overcast).

industry costs. Applying Dr. Lowry's X-Factor calibration approach in the manner that he has done elsewhere would significantly reduce his recommended X-Factors to a level closer to zero, even without accounting for the other errors identified above.

241. Dr. Overcast observed "a fundamental disconnect between the text and the discussion of appropriate calibration [in Dr. Lowry's Evidence] and the actual TFP recommendations."[399] Dr. Lowry states in his Evidence that "when a macroeconomic inflation measure is used, the ARM [Attrition Relief Mechanism] must be calibrated in a special way if it is to reflect industry cost trends… [and that] … the inflation measure can still conform to index logic provided that the X factor effectively corrects for any tendency of GDPPI growth to differ from industry input price growth."[400] Dr. Overcast explained how calibration works under Dr. Lowry's approach:

> According to the theory that PEG is employing, calibration of the X-factor depends on the relationship between a 'productivity differential' and an 'input price differential', each of which exert upward and/or downward pressure on the X-Factor depending on certain conditions. The summation of these two differentials determines the appropriate X-Factor that is warranted when a macroeconomic inflation measure is used. As such, both differentials need to be considered in light of one another in order to appropriately conclude whether an argument for a positive or negative adjustment of the X-factor exists.[401]

242. Dr. Lowry concluded that no downward calibration was required; however, he arrived at that conclusion by only examining the Productivity Differential, without considering the Input Price Differential.

243. Dr. Lowry provided, in response to an IR, a rationale for not incorporating a downward adjustment in this case. However, Dr. Overcast demonstrated in his Rebuttal Evidence why each of Dr. Lowry's reasons was without merit.[402] Dr. Lowry had incorporated a

---

[399] Exhibit B-45, Overcast Rebuttal Evidence, p.53.

[400] FEI Exhibit C1-9-1, Errata to Lowry Evidence, p.13. For clarity, the 'index logic' to which PEG is referring is the 'revenue per customer index' and 'GDPPI' is the example of a macroeconomic inflation indicator used.

[401] Exhibit B-45, Overcast Rebuttal Evidence, pp.54-55.

[402] Exhibit B-45, Overcast Rebuttal Evidence, pp.59-60.

downward adjustment in other proceedings in similar circumstances. As Dr. Overcast put it, "PEG's recommendation against adjusting the X-Factor in this proceeding is also the polar opposite of what he has advocated in other proceedings."

244. Dr. Overcast completed the calibration analysis based on how Dr. Lowry had applied it elsewhere. It yielded a material negative adjustment.[403] The proper and complete application of Dr. Lowry's calibration logic and formula yields the following results:

- When TFP growth of the industry for capital is 1.34% and the BC-GDPIPI is used as the sole macroeconomic inflation measure, a calibrated X-Factor of 0.14% including stretch ensures that the X is reflective of industry costs. This is in contrast to Dr. Lowry's recommendation of 1.54% in this scenario.[404]

- When TFP growth of the industry for capital is 1.05% and the BC-GDPIPI is used as the sole macroeconomic inflation measure, a calibrated X-Factor of -0.12% ensures that the X is reflective of industry costs. This is in contrast to Dr. Lowry's recommendation of 1.25% in this scenario.[405]

Undertaking only the calibration that Dr. Lowry says is necessary, based on his own calibration methodology, results in his X-Factor being significantly lower than that proposed by FBC and FEI and more consistent with the B&V recommendation of a zero X-Factor.[406]

(f) Upward Bias is Not Offset By Other Factors

245. Dr. Lowry acknowledged at the hearing that in order for the ultimate recommendation that he put forward to be useful, "the approximations of reality have to really

---

[403] Exhibit B-45, Overcast Rebuttal Evidence, p.56: "A quick comparison of the Productivity Differential of 1.58% and the Input Price Differential of 1.74% indicates that the downward calibration of the X-Factor suggested by the Input Price Differential more than offsets the upward calibration of the X-factor suggested by the Productivity Differential. As such, there is a clear argument for a negative X factor adjustment according to PEG's evidence and to the methodology used previously by PEG."

[404] Exhibit B-45, Overcast Rebuttal Evidence, p.61.

[405] Exhibit B-45, Overcast Rebuttal Evidence, p.62.

[406] Exhibit B-45, Overcast Rebuttal Evidence, p.53.

be approximations of reality" at least to the extent that "they have to be a reasonable approximation on average" or there are offsetting factors.[407] Dr. Lowry seemed to suggest that BC-CPI is overstated by up to 50 basis points, and that this cancels out any upward bias in his TFP calculations. The trouble with this argument is that, as demonstrated above, the upward bias in Dr. Lowry's TFP calculations is much larger than any potential upward bias in the composite I-Factor associated with one of the components being upward biased. All of his indexes incorporate upward bias, and the amount of upward bias is significant. Dr. Overcast summed up as follows:

> And I think the confusion arises because all studies, whether they're PEG's or mine, must make assumptions to reflect the real world in their measures of deflators and price indexes.
>
> The deflators and price indexes applied in determining the quantity index suffer from something that's known in technical terms as substitution bias. And that's because they're fixed-base index, and we talked about that today. You understood that the Handy-Whitman index, for example, is fixed base 1973. And that's for both gas and electric.
>
> Now, the idea of substitution bias, if I can, let me just explain it to you in sort of a simple example. And in fact Dr. Lowry mentioned that the CPI as a measure of inflation is biased. And he pointed out that that number was .5, and it's largely driven by substitution bias. But here's the way it works. When you set the base, let's suppose that everybody was eating a lot of steak. So it was -- it had a high weight in the budget. And because of subsequent events, people have stopped eating as much steak and they have substituted chicken. All right, with a fixed-weight index, as the price of steak continues to go up, it's got a higher weight, and chicken's got a lower rate, even though people are now consuming more of it. And so if the CPI was going to really track what would happen, you would be changing the CPI to give chicken a higher weight in determining how inflation is reflected in the index.
>
> The critical problem in all of this analysis is that this substitution bias is much larger in the indexes that PEG uses, and I'm going to discuss that below. And the net result is that PEG's results are consistently producing TFPs much higher than the actual TFP which probably should be somewhere in the neighbourhood of zero to some negative number. And simply, you just can't accept my numbers or

[407] T7:1393, l.22-1394, l.5 (Lowry); T7:1395, ll.18-21 (Lowry).

> his at face value, because they all have these assumptions built in. And you have to recognize that those values have to be adjusted for these biases.
>
> And for -- in the case of PEG's analysis, all of their indexes have this problem, and the problem all works in one direction. It makes their estimates higher, and I'm going to show you that in a minute as well.[408]

246. The adjustment for the use of plastic pipe for gas utilities alone represents 165 basis points, which dwarfs the 50 basis points that Dr. Lowry identified for CPI. On top of that, Dr. Lowry's exclusion of 66% of assets with service value as a result of his approach to depreciation results in underestimating capital imputs required to produce an output "by an amount that's orders of magnitude -- we're not talking about tiny differences now, we're talking about big differences."[409] There is no question that Dr. Lowry's TFP is materially overstated.

(g) Approach to Adjusting Measured TFP to Account for Exclusion of CPCN Capital from Formula

247. Dr. Lowry agreed with Dr. Overcast that, in arriving at a final X-Factor recommendation for FortisBC, the "raw" TFP results should be adjusted to account for the exclusion of CPCN capital from FortisBC's proposed formula. Dr. Lowry had initially appeared to provide in his written evidence an X-Factor sensitivity analysis based on certain percentages of capital being excluded; however, he later underscored that the calculations were illustrative and did not reflect an accepted methodology for making adjustments.[410] Dr. Lowry conceded that "No X factor has to Dr. Lowry's knowledge been approved on the basis of this methodology."[411] He indicated that he "wasn't comfortable that that was the reasonable thing to do" and "But as you may have noticed, at the end, I didn't actually -- when I proposed any

---

[408] T7:1500, l.9-1502, l.1 (Overcast).

[409] T7:1521, l.3-1523, l.1 (Overcast).

[410] FEI Exhibit C1-22, BCUC-CEC (Lowry) IR 2.13.1: "These calculations were provided for illustrative purposes only. There is no established method for adjusting X to eliminate the intertemporal overcompensation that can result when a capital tracker is added to a PBR plan featuring a single ARM such as a rate or revenue cap index."

[411] FBC Exhibit C6-13, BCSEA-CEC (Lowry) IR 1.12.1.

specific upward adjustment to the X, because I just wasn't confident that we'd found a number that we could hang our hat on."[412]

248. Dr. Overcast explained why it is not possible to model the impact of CPCN capital by simply reducing the annual capital expenditures by a specific percentage reduction each year:

> CPCN typically represents capacity upgrades in the existing system or system expansions that add lumpy capacity to serve new customers. Capacity outputs, of course, are not measured by PEG in their report. PEG makes no adjustment to the measure of output (the number of customers) which means that PEG assumes that the reduction percentage does not impact the number of customers served. This is not a sound assumption when the percentage of new capital costs is between 70% and 80% for mains and services and that does not include meters and regulators. This means that there is no reasonable alternative to modeling CPCN without reducing the resulting output as measured by new customers in the PEG report. This is an example where the assumptions underlying the results are physically impossible and thus the increase in TFP is meaningless. Finally, there may be cases where the capacity added by the CPCN project is not justified on the need for capacity but the ability to reduce the costs for fuel or to access lower cost gas supplies. This means that CPCN in any form is not able to be reflected in the TFP study by arbitrarily reducing the capital costs.[413]

The Commission should determine, based on Dr. Overcast's evidence discussed earlier in this Part of the PBR Submission, that there is no established formula or methodology for accounting for the impact of CPCN capital on TFP.[414]

249. In the end, Dr. Lowry did not recommend a specific adjustment. Dr. Overcast's approach is reasonable and the Commission should accept that a zero X-Factor would account for an appropriate judgment-based adjustment.

---

[412] T7:1486, ll.1-26 (Lowry).

[413] Exhibit B-45, Overcast Rebuttal Evidence, pp.31-32. See also: T4:624, l.11-625, l.11 (Overcast).

[414] Exhibit B-45, Overcast Rebuttal Evidence, pp.31-32; FEI Exhibit C1-22, BCUC-CEC (Lowry) IR 2.13.1.

(h) Conclusion Regarding Issues With Dr. Lowry's Methodology

250. Dr. Overcast has identified a number of areas where the assumptions that Dr. Lowry has used in his index-based approach do not make sense for utilities and systematically make the electric and gas utility industries appear more productive than they really are.[415] Dr. Overcast's approach of using actual *ex post* costs and deriving a central tendency was specifically intended to address problems inherent with using an index-based approach that produces significant upward bias when applied to utilities. Dr. Overcast's approach isn't perfect either,[416] but it is far more robust than a measure that requires numerous assumptions that cannot be supported based on the evidence.

E. CONCLUSION REGARDING THE PBR FORMULA

251. The I-X Formula is a critical element of the proposed PBR Plan. FortisBC submits that evidence supports the use of the proposed composite I-Factor and the proposed X-Factor of 0.5%. The proposed X-Factor is much higher than what Dr. Overcast's analysis would suggest, and is supported by what is occurring in the industries, the Ontario PEG results, a comparison against five-year forecasts and the Companies' long history under PBR. It is also consistent with what Dr. Lowry's approach would likely yield (i.e., a negative X-Factor) if the necessary calibration and adjustments were made.[417] The proposed I-X formula reflects the Companies' commitment to provide immediate benefits to customers under PBR by accepting an appropriate productivity challenge. The formula should be approved as proposed as part of the overall PBR Plan.

---

[415] A summary of the issues with Dr. Lowry's approach is included in Exhibit B-45, Overcast Rebuttal Evidence, p.71.

[416] Dr. Overcast stated at p.65 of his Rebuttal Evidence (Exhibit B-45): "Better data would improve the precision of the estimates but is unlikely to be practical since the requirements would be substantially more costly as standardized reporting requirements and would be of minimal value except as it relates to developing measures of productivity."

[417] Exhibit B-45, Overcast Rebuttal Evidence, p.71; T7:1528, ll.6-22 (Overcast).

PART FIVE: MAINTAINING SERVICE QUALITY

252. The Companies have a track record of maintaining a consistently high level of service quality, both under PBR and under COS regulation. FortisBC designed the PBR Plan with an understanding and acceptance of service quality at the existing high levels. There has never been an instance where these Companies, under their current ownership, have been found to have taken some action or made a decision aimed at enhancing profits at the expense of service quality.[418] FortisBC's credibility with the Commission and customers - credibility that FortisBC must draw upon every time the Companies come before the Commission - depends on continuing to place a high priority on maintaining service quality under this PBR Plan. FortisBC's performance will be reviewed annually. The Commission has prescribed enforcement powers, which now include administrative penalties in the event that the Commission were to make an order regarding SQIs and FortisBC did not comply with it. All things considered, the notion that the Companies will suddenly begin sacrificing service quality to generate short-term earnings under this PBR is only a theoretical risk.

253. The following points, discussed in this Part, should be considered in light of the above context:

- First, SQIs should be designed to maintain the existing high level of service quality, not to require even higher service levels at additional cost to customers.
- Second, the suite of SQIs proposed by FortisBC is appropriate for providing an indication of the overall customer experience.
- Third, the Annual Review and Mid-term Review processes, in conjunction with established regulatory mechanisms, can be used to respond to any decline in service quality.

[418] Mr. Swanson noted starting at T3:377, l.14 that FBC's previous owner had presided over service declines, which Fortis Inc. committed upon acquisition to rectify. FBC has since invested significantly to meet those commitments.

- Fourth, the Commission should not entertain Ms. Alexander's heavy-handed and arbitrary approach that neither aligns with FortisBC's demonstrated commitment to providing high levels of service, nor abides by the procedural safeguards inherent in the UCA.

A. SQIS INTENDED TO MAINTAIN SERVICE QUALITY, NOT INCREASE IT

254. The Companies already maintain a high standard of service. The focus of the SQIs should be on maintaining the existing high level of service quality, not (as COPE's witness suggests) on increasing service levels at additional cost to customers.

255. The Companies have reported to the Commission on service quality for many years. The utilities only recently completed litigated revenue requirements proceedings to establish 2012 and 2013 rates. The Commission has been kept fully apprised of the existing service levels for both Companies, and considered the Companies' revenue requirements in light of those service levels. The Commission has not identified any shortcomings in service quality in recent decisions. Those decisions also make no mention of customers demanding higher service levels. To the contrary, in FBC's 2012-13 RRA Application BCPSO had argued "that it is important to strike a balance between safety, reliability, quality of service and achieving reasonable customer rates."[419] The Commission agreed with BCPSO and went on to say: "Taking this into consideration, the Commission Panel is of the view that safety, reliability and quality of service to ratepayers are at an acceptable level and a focus on identified problem areas is considered most appropriate at this time." The Commission also noted that some of FBC's proposed transmission sustainment projects were based on line condition assessments where the lines themselves had good reliability, and suggested that FBC might be setting the condition threshold too high for some of the projects.[420] There is nothing inherent in moving to PBR from cost of service regulation that would require attaining higher service levels than

[419] FBC 2012-2013 RRA Decision, p.91.

[420] FBC 2012-2013 RRA Decision, pp.96-98.

existed in 2012-2013; if service levels were satisfactory in 2012-2013 that is strong evidence to suggest that they remain satisfactory.

256. Ms. Alexander never assessed the implications of her recommendations ("I have not the capacity, nor have I attempted to predict the cost implications…").[421] She didn't consider whether customers wanted or needed higher service levels ("And when I say "customer needs" [regarding TSF], I'm not referring to a survey, or my knowledge of any particular data, from your service territory").[422] This isn't surprising. Ms. Alexander considered that it was the shareholder's responsibility under PBR to absorb any cost associated with providing higher service levels.[423] In taking this view, Ms. Alexander has misapplied the UCA. If the Commission considers that higher service levels are required, the base year costs must be adjusted accordingly. Customers must also pay to maintain those service levels once PBR is over.

257. Ms. Alexander's whole approach to SQIs seems to have been premised on FortisBC being a utility with chronically poor service, with a track record of prioritizing short-term earnings above its ability to recover its return on and of capital over the long-term. While that may be her experience in the United States, it isn't applicable in BC. FortisBC submits that the existing high service levels continue to be appropriate. Requiring even higher service levels, particularly when combined with significant financial consequences for a decline in service quality from those elevated levels, would introduce an asymmetrical risk for the utility and would alter the nature of the PBR proposal in a meaningful way.

B. THE APPROPRIATE SUITE OF SQIs

258. The Companies' proposed SQIs are addressed in FBC Appendix D6 and FEI Appendix D7. In developing the proposed SQIs, FortisBC reviewed its experience with the existing indicators, customer research and service quality indicators used by other Canadian

[421] FEI Exhibit C2-10, Alexander Evidence, p.15, 22-42; T5:921, ll.22-25 (Alexander).
[422] T5:931, l.26-932, l.2 (Alexander).
[423] T5:925, ll.11-19 (Alexander).

utilities.[424] The suite of SQIs is similar to the indicators used by the Companies in previous years.[425] The proposed benchmarks, where applicable, typically reflect either industry standards or the Company's performance over recent prior periods.[426] FortisBC submits that the suite of SQIs and the proposed benchmarks provide a sound basis for assessing the overall customer experience during PBR. FortisBC addresses below the main issues raised with respect to individual SQIs; any other issues raised will be addressed in Reply Submissions.

Telephone Service Factor

259. Telephone service factor ("TSF") is a measurement of the percentage of non-emergency calls answered within a defined window of time and was previously called "Speed of Answer". A TSF of 70/30 represents a high level of customer service. While COPE wants to see a higher level of non-emergency service from the call centre (80/30), it is important that the Commission keep in mind that COPE's interest in increasing the amount of available call centre work for its members is not aligned with the interests of customers.

260. Mr. Loski explained that increasing the TSF to 80/30 will increase costs and reduce labour productivity:

> …a higher TSF means more resources are available to answer calls, and a lower TSF translates into lower resources levels and therefore lower cost. So the math behind the telephone service factor is something, a formula call the Erlang C model or formula, we had, I believe, reference to that in our rebuttal evidence which was FEI Exhibit B-47 at page 3, question 5.
>
> The other really interesting thing that also is a product of this model is what's called in the contact centre arena, agent occupancy, which looks at -- it's a -- it just simply looks at the arrival rate. Again, it's that number of calls within that interval as then the numerator, and the denominator is the number of agents. So if you increase the number of agents, which would be the result of increasing the service level, you actually end up with a different occupancy level, meaning your agents are going to be less occupied if you're increasing that service level.

[424] FEI Exhibit B-1-3, FEI Application Evidentiary Update, Appendix D7, p.1.

[425] T2:243, ll.11-16 (Swanson).

[426] FEI Exhibit B-1-3, FEI Application Evidentiary Update, Appendix D7, p.2.

> Meaning occupancy is, in the contact centre arena, is the measure of productivity of your agents.
>
> So by increasing your telephone service factor, you actually are decreasing the productivity of your agents. And so, what we -- when we looked at our telephone service level, we've got 70 percent in 30 seconds for our electric customers and we've been -- we believe that our customers are of the view that that's a reasonable target. And again, that's a good balance of service quality and cost.
>
> And so we're of the view that our gas customers would have the same view of that balance of costs and quality. And we know we've heard a lot from our customers and through the various regulatory processes that we want to see, you know, keep cost increases down and improve productivity. And by going to a 70/30 telephone service factor for our gas customers and maintaining that for our electric customers, we believe is a good measure, then, of cost savings as well as maintaining good service quality and enhancing productivity.[427]

261. There is no logic to increasing the TSF to 80/30, at a greater cost and lower labour productivity, when:

- FortisBC does not "get any material number of customer complaints with respect to the length of time that they have to wait."[428]
- the average speed of answer is about 42 seconds; [429]
- call abandonment rates are low for the industry, a compelling indication that FortisBC customers are prepared to wait until their call can be addressed by a live agent;[430] and
- Mr. Loski's well-informed view is that "the speed that we answer the phone, whether it's in 25 seconds or 50 seconds, is not the most important thing to our

[427] T5:1091, l.12-1094, l.23 (Loski).

[428] T6:1157, ll.3-8 (Loski).

[429] T5:1096, l.21-1097, l.3 (Loski).

[430] T6:1275, ll.11-21 (Loski); T5:1018, ll.5-10 (Alexander).

customers when they are contacting. The most important thing to them is that we resolve the issue for their call."[431]

The latter point takes us to First Contact Resolution.

First Contact Resolution

262. FortisBC has proposed a First Contact Resolution ("FCR") metric. There are two reasons why including FCR in the suite of SQIs makes sense:

- First, research discussed in the Application indicates that for every one percent improvement in FCR, there is typically a one percent improvement in customer satisfaction (top box response), all else being equal. Their research supports that FCR is the metric with the highest correlation to customer satisfaction. This conclusion is affirmed through statistical analysis of FBC's own electric customer service survey data.

- Second, improved FCR also means fewer repeat calls, lower volumes, and (other things being equal) lower staffing requirements in the call centre. From the perspective of customers and the Companies, lower operating costs associated with lower labour costs, and satisfied customers, is a "win-win" situation.[432]

263. Ms. Alexander's stated reason for opposing FCR is that she does not believe customers understand that they can dispute the answer they receive from the call centre agent.[433] When Ms. Alexander was asked about the basis for her suspicion, she replied:

> And I don't know the answer to that question. But I must say, I looked at the customer complaint numbers in this proceeding and was shocked at how few there are. This is not a reflection of a customer base that knows how to dispute payment arrangement terms, disconnection of service, quality of service, and so forth. This is not typical. And I didn't make any statements about that in my

[431] T6:1114, l.22-1115, l.1 (Loski).

[432] T6:1142, l.4-1143, l.15 (Loski); T5:977, ll.7-11 (Alexander).

[433] FEI Exhibit C2-10, Alexander Evidence, p.33.

> testimony, but you're pushing me in that direction here, so -- I had a concern about it.[434]

Ms. Alexander admitted that she has "no evidence to suggest that's the case".[435] A more likely explanation in light of the Companies' already high level of service quality is simply that customer concerns are generally being addressed. There is no evidence that would justify assuming otherwise.

264. Ms. Alexander's rejection of a metric that would encourage prompt resolution of customer complaints serves only the interest of COPE.

Billing Accuracy and Meter Reading Accuracy

265. Ms. Alexander has proposed doing away with Billing Accuracy and Meter Reading Accuracy metrics - the two other mechanisms (along with First Call Resolution) where higher performance drives down call-centre labour costs. Customer concerns about billing and meter-reading accuracy drive call volumes at the call centre.[436] While Ms. Alexander is correct that the Companies maintain high levels of service already, maintaining high levels of Billing Accuracy and Meter Reading Accuracy have a favourable influence on costs and encouraging it should be of interest to customers.

Customer Satisfaction Index ("CSI")

266. The Companies propose to use the CSI results as a directional indicator, consistent with how this measure has been used in past FEI PBRs. The proposed approach is appropriate because customer attitudes are often influenced by factors outside the Company's control. The price of natural gas can have an adverse influence on FEI's customer satisfaction. FBC's customer satisfaction appears to have been influenced recently by the Commission-

[434] T5:979, ll.10-20 (Alexander).

[435] T5:1021, ll.19-22 (Alexander).

[436] T5:975, l.5-976, l.5 (Alexander); T5:1085, ll.19-25 (Loski).

initiated Residential Conservation Rate, AMI project, and electricity rates in general. As a result, trend information is more valuable and useful than the actual quarterly number.[437]

All Injury Frequency Rate ("AIFR")

267. AIFR is a key metric internally given FortisBC's focus on employee safety. It is included in the suite of SQIs to demonstrate the Companies' safety focus, but it should be a directional measure.[438] First, the goal for on-the-job injuries is zero. As Mr. Swanson explained: "Safety is a classic example where we strive to have zero incidents. So just because our target is set at a number that includes a certain number of incidents, we don't just stop there."[439] Second, AIFR is only tangentially related to the customer's overall experience. Third, there is a safety and compliance regime and regulator that oversees employee safety.

Public Contact With Pipelines

268. FEI is proposing this metric as a directional measure, without a specific benchmark. Ms. Alexander has proposed a specific benchmark, determined by rolling three-year average. There are two major problems with her approach. First, although FEI places significant attention on educating the public of the risk associated with gas line contact, the results of this SQI are beyond FEI's direct control. There is no mechanism to compel the public to contact FEI for a pipeline location. Some individuals, companies and contractors will disregard "call before you dig" advertising. Second, even if a benchmark were to be established, using a three year average would cause any benchmark to lag during improving economic conditions.[440] This metric was informational in the last FEI PBR, and should remain so.

---

[437] FEI Exhibit B-1-3, FEI Application Evidentiary Update, Appendix D7, p.14; FBC Exhibit B-1-1, FBC Application, Appendix D6, p.10-11.

[438] FEI Exhibit B-1-3, FEI Application Evidentiary Update, Appendix D7, p.12; FBC Exhibit B-1-1, FBC Application, Appendix D6, pp.9-10.

[439] T6:1121, l.24-1222, l.2 (Swanson).

[440] T5:961, ll.7-1: Ms. Alexander admitted "I have made no specific connection between my calculation and the economic ups and downs of the construction industry in your service territory, sir."

SAIDI/SAIFI

269. FBC proposes to continue measuring transmission and distribution system reliability (SAIDI[441] and SAIFI[442]) as adjusted by the Institute of Electrical and Electronics Engineers (IEEE) method of normalizing reliability statistics by excluding "major events".[443] FBC proposed to include this metric as an informational SQI.[444]

270. A directional measure is appropriate for SAIDI and SAIFI. Mr. Chernikhowsky noted that "outages will occur". Significant events happen that are below a threshold for normalization.[445] Response times are affected by the rural and isolated nature of some parts of the system.[446] It is not possible to fix all of the problems in the system at once, so the utility attempts to "deploy dollars optimally to balance safety, cost and reliability".[447]

271. Ms. Alexander recommended a benchmark based on the three-year average. She gave no account to the fact that using average performance generally contemplates that the level of performance will sometimes be lower than the benchmark, stating: "The company would have to manage to meet the proposed standard. Whatever the standard is, it has to have some meaning. Either meet it or you don't."[448] This approach effectively requires that FBC must manage to a much higher level of reliability than it does today if it is to avoid

---

[441] SAIDI is the amount of time the average customer's power is off per year (i.e. the total amount of time the average customer's clock would lose during a year). FBC Exhibit B-1-1, FBC Application, Appendix D6, p.8.

[442] SAIFI is the average number of interruptions per customer served per year (i.e. the number of times the average customer would have to reset their clock during the year). FBC Exhibit B-1-1, FBC Application, Appendix D6, p.8.

[443] Major events are identified as those that cause outages exceeding a threshold number of customer-interruptions or customer-hours. Threshold values are calculated by applying a statistical method called the "2.5 Beta" adjustment to historical reliability data. FBC Exhibit B-1-1, FBC Application, Appendix D6, p.8.

[444] T5:1047, l.21-1048, l.20 (Swanson).

[445] T5:1054, l.13-1055, l.5 (Chernikhowsky) .

[446] The response to FBC Exhibit B-25, CEC-FBC IR 2.49.5 quantifies to costs to improve response time, and notes that four rural and isolated regions (Princeton, Kaslo, Creston, and Grand Forks) in the service territory would require additional staff to complement existing crews. Ms. Alexander did not consider how the Companies could increase performance in terms of shortening the duration of outages without adding additional personnel to rural areas: T5:955, l.6-956, l.1.

[447] T5:1060, l.14-1061, l.6 (Chernikhowsky).

[448] T5:940, ll.1-4 (Alexander).

penalties when downward variances occur. Ms. Alexander's approach ignores the practical realities of maintaining utility infrastructure. FBC cannot possibly upgrade all of its systems immediately; investments must be prioritized. For that reason, FBC's infrastructure investments do not typically target reliability *per se* - reliability is an outcome of projects driven by other imperatives.[449] In past FBC applications, as described above, customers have expressed concern about the need to balance reliability with cost. The Commission agreed.[450]

272. We discussed in Part 4 the professional and regulatory requirements that dictate the Companies' ongoing maintenance of capital assets. This will continue irrespective of the existence of a specific benchmark for SAIDI and SAIFI. Mr. Chernikhowsky also explained that there are financial consequences for the utility associated with declines in these metrics: "Those customers have to get put back on when they have the outage. And so the utility will incur costs, both operating and capital, to restore them."[451]

273. In light of all of these factors, FBC's proposal to continue to treat SAIDI/SAIFI as directional measures is appropriate.

Rationale for Eliminating SQI for Generator Forced Outage

274. FBC has proposed to eliminate the Generator Forced Outage Rate ("FOR"), which was included in the 2007 Plan, because FOR does not impact customer service. Mr. Chernikhowsky explained:

> [G]enerator reliability does not actually impact customers, and the reason why is because our fleet of generating units actually is a small portion of the resources that we draw on to supply customers. And in fact, we could use [sic - lose] all of our generating units and our customers would still not actually experience an outage.
>
> So, it goes back to when we were looking at the portfolio of SQIs that we were putting together, we were looking at ones that best represented what the

[449] T5:1057, l.20-1058, l.5 (Chernikhowsky mis-attributed to Swanson).

[450] FBC 2012-2013 RRA Decision, p.91.

[451] T5:1064, ll.1-9 (Chernikhowsky).

> customers would value, and so because the generator forced outage rate does not directly impact them, we didn't put it forth this time around.[452]

Mr. Chernikhowsky's explanation is compelling and FBC's proposal should be accepted.

SQI For Asset Integrity Would Be Redundant

275. FortisBC did not propose an SQI relating to asset integrity. Mr. Swanson characterized FortisBC's position on an asset integrity benchmark as follows: "I don't think we would be opposed to it. We just don't know if the value would be there to add it. So when we look at the duplicative nature of the reporting, when we look at the tie to the service quality, we just don't think it met the criteria that we've laid out there."[453] Mr. Swanson was referring in the first instance to the significant compliance reporting already being undertaken by the Companies. Mr. Pataki indicated, for instance, that FEI undertakes the following reporting:

> …I'd like to add to Mr. Chernikhowsky's comments that we already provide the Commission this detailed reporting on the transmission assets of FortisBC Gas. We have a transmission pipeline integrity report that's filed with the Commission on an annual basis. We meet with the Commission to review the contents of that document, and that document itself and the meetings that go with it I think are way more valuable than any one indicator could provide. I think the Commission receives way more value out of that process than an indicator would provide. [454]

Mr. Chernikhowsky spoke to the difficulty of establishing a reliable short-term benchmark for asset integrity when deterioration in asset health tends to lag over a longer time period.[455]

C. CONSEQUENCES IN THE EVENT THAT PERFORMANCE DECLINES

276. One of the themes during the hearing was that FortisBC's SQI proposal lacked enforceable consequences, and that this should be a cause for concern. As indicated above, there is no evidence that the Companies, under their current ownership, have ever taken

[452] T6:1260, l.17-1261, l.9 (Chernikhowsky).

[453] T6:1199, ll.14-20 (Swanson).

[454] T6:1198, l.26-1199, l.11 (Pataki).

[455] T6:1198, ll.4-19 (Chernikhowsky).

actions or made decisions that sacrificed service quality to generate short-term profits. FortisBC's witnesses have repeatedly indicated that they have every intention of managing the business so as to maintain existing service levels. The Commission should give significant weight to all of that evidence, and adopt an approach to enforcement that is consistent with it. We make the following points below:

- First, there is a difference between SQI results that are below a benchmark and declining service quality;
- Second, the Commission has recourse to existing regulatory mechanisms in the event of a service quality decline;
- Third, adopting Ms. Alexander's proposal for automatic and arbitrary penalties would be both unfair and unlawful; and
- Fourth, if the Commission considers it to be necessary to specify a process beyond the process that is already available to it under the UCA, the Commission should proceed with caution to ensure that the PBR Plan remains fair to the Companies as well as customers.

(a) Defining Declining Service Quality

277. The Commission should interpret and enforce SQIs with the recognition that there is a difference between SQI results that are below a benchmark and declining service quality. First, volatility in service quality is to be expected, irrespective of the actions of FortisBC. Dr. Overcast expressed this point at the hearing as follows:

> …the SQIs are statistics. And by their very nature, statistics are going to change up and down over time. I mean, let's take SAIDI or SAIFI. I mean, once you excluded the specifically defined -- I can't think of the right word. I'm sure somebody down there -- but you exclude some things because they're like catastrophic, you know. They hit everybody, and those numbers are taken out before you count SAIDI and SAIFI. But there is no exclusion, for example, for the fact that one season you have a hundred thunderstorms, in another season you have 35.

> I mean, you know, just by nature, weather is very variable, and that's one of the drivers of the frequency and the duration of interruptions. And so if you say, well, we're going to hold you to this number, well, you know just by law of averages that that number, there's going to be numbers all around that number. And to the extent you have more storms one year the number would go up, you have less storms the next year the number would go down. Trying to tie that to a specific penalty seems to me to miss the point.
>
> The point of these is to try to give you a baseline that says the company is not changing that baseline in order to profit by its reducing those factors.[456]

A benchmark based on a historic average necessarily contemplates that performance will be below the benchmark part of the time. Second, survey results that are used in determining Customer Satisfaction and First Call Resolution, for instance, are also subject to a statistical margin of error. Third, the overall customer experience extends beyond the results of a single SQI. Lower results for an individual SQI should be considered in light of the results for the entire suite of SQIs It would be highly artificial to treat each SQI in isolation, ignoring all other results, as Ms. Alexander's approach requires.

(b) Regulatory Mechanisms Already Available to Commission

278. During the course of the hearing, the Commission invited the Companies to lay out their position regarding SQI and off-ramps in this PBR Submission:

> COMMISSIONER COTE: Q: I have just got to add to what Commissioner MacMurchy said. A comment or a request from the -- and I think I am speaking from the whole panel that with regards to a lot of today, that a lot has been said about the position of Fortis, yourselves, with -- and Ms. Alexander with regards to the penalties for failure to meet the SQIs.
>
> On the one hand, you've got sort of the Fortis position where SQI scores are laid out, and the panel has the option to sort of drop the neutron bomb, I think, is the terminology that's been used. In other words, cancelling a PBR if we're dissatisfied with the kind of results we're getting.

[456] T6:1222, l.21-1223, l.22 (Overcast). See also: Exhibit B2-8, BCUC-FEI/FBC IR 3.25.3.

> On the other hand, you've got a detailed process that Ms. Alexander has laid out, re the administration of penalties for failure to reach. Over the course of -- especially this morning, various interveners have explored some of the territory that lies in between. And I have to admit, I have a fair number of questions in that regard. But I don't think we want to add to this, because there is a fair amount of ground that's already been covered.
>
> However, the request from the Panel is, to the extent that Fortis might have changed its position, or would like to clarify its position as to how this would work specifically, I would very much appreciate it. And if you would undertake that in argument, and lay it out so we're real clear on where you stand and how it's going to work, and we know what we're dealing with.[457]

FortisBC appreciates the Panel's invitation to clarify its position, as FortisBC would not frame its position or the parameters of the debate in quite the same way. In particular, there is recourse for customers and the Commission under FortisBC's proposal apart from triggering an off-ramp (which Mr. Quail colourfully dubbed the "bomb"). FortisBC took for granted in developing its proposed PBR Plan that there are statutory mechanisms available to address service quality declines.

279. As outlined in the Applications, the Companies must report to the Commission and interveners on the SQI results during the Annual Review process, and explain any failure to meet a specific SQI result.[458] There are two possible outcomes in such circumstances:

- ***A finding that the decline in service is attributable to factors beyond the Companies' control***: In this situation, the Commission can elect to do nothing, or establish monitoring and reporting requirements, for instance. It would be inappropriate to take further action against FortisBC in circumstances where the Companies were acting prudently.

[457] T6:1273, l.19-1274, l.23.

[458] FEI Exhibit B-1-3, FEI Application Evidentiary Update, Appendix D7, p.17; FBC Exhibit B-1-1, FBC Application, Appendix D6, p.13; T6:1201, l.19-1203, l.2 (Loski).

- ***A finding that some action of FortisBC directly caused or contributed to the decline***: In this situation, the Commission has other options open to it. The Commission's powers under the UCA include:

    - The ability to order FortisBC to take certain steps to address service quality;[459] and

    - The power to levy administrative penalties after a hearing if the Companies breach the Commission order.[460]

280. The same process is available to stakeholders and the Commission under COS regulation, and under PBR the Companies are reporting more frequently. The above process is the epitome of specific, enforceable consequences.[461] It is also the most specific enforcement mechanism that any SQI framework can stipulate in advance, given the requirements under the UCA for levying administrative penalties and rules of natural justice discussed in the next section.

(c) Ms. Alexander's Penalty Recommendations Should Be Rejected

281. Ms. Alexander's recommendations suffer from a number of flaws that were discussed in FortisBC's Rebuttal Evidence, Dr. Overcast's Rebuttal Evidence, and at the hearing. Below, we first explain the flawed premise underlying Ms. Alexander's approach, and then address why Ms. Alexander's penalty proposal would be unlawful and could not be adopted.

Ms. Alexander's Flawed Premise

282. The whole premise of Ms. Alexander's penalty recommendations is fundamentally flawed in two material respects.

---

[459] Sections 42 and 73.

[460] Sections 109.1 and 109.2. Mr. Swanson addressed these mechanisms at the hearing, stating: "You know, we have the Commission who has the right to make orders if they feel we are not acting at an appropriate level. You know, administrative penalties tied to those -- to those orders and our adherence to them." T5:1063, ll.9-13 (Swanson).

[461] T6:1224, ll.9-19 (Overcast).

283. First, the rationale for her recommendations is that "Utilities should not earn incentives for doing their job. The purpose of this SQI with penalties is to right the balance in light of the earnings potential and incentives under the PBR."[462] This is a flawed premise because Companies "do their job" in a similar fashion under both COS and PBR rate regimes. As explained earlier, PBR is about generating benefits for both customers and the Companies by increasing the opportunities for cost-effective investments in efficiencies. Customers receive an immediate benefit from the use of a formula that incorporates a productivity improvement (X) factor. Ms. Alexander's articulation of the purpose of her penalty regime suggests that she is attempting to transfer benefits achieved under the PBR from the Companies to customers, rather than trying to ensure that service quality is not compromised by the utility in its efforts to seek out savings. This inference is supported by the fact that:

- Ms. Alexander reached her conclusion that she needed to "right the balance" without ever having reviewed the overall PBR Plan proposal;[463] and

- The Companies would be subject to immediate and significant penalties under her proposal (the magnitude of which is reflected in Staff's witness aid marked Exhibit A2-29) for meeting the standard of service that, to this point, has been acceptable to the Commission and customer groups.[464]

284. Second, it is evident that Ms. Alexander perceives due process as a nuisance that causes time and expense where "witnesses come here and tell you all the sob stories about how they weren't in control of this and it didn't happen on their watch and they're very sorry and it won't happen again, and it was just 1 percent and so who cares."[465] FortisBC submits that all of those factors that Ms. Alexander has identified (pejoratively) would be relevant and

---

[462] FEI Exhibit C12-3, Alexander Opening Statement, p.4.

[463] FEI Exhibit C12-3, Alexander Opening Statement, p.4; T5:910, l.5-911, l.3 (Alexander).

[464] SAIFI and SAIDI, for example, T5:946, l.22-947, l.3 (Alexander). As the economy recovers, pipeline strikes will also likely increase: T5:959, ll.15-23 (Alexander).

[465] T5:997, l.12-998, l.7 (Alexander).

important considerations in any assessment of administrative penalties under the UCA, and the fact that her recommendations do not abide by them is fatal to her approach.

No Consideration of Causation and Prudence When Quality Declines

285. Utilities must be permitted to recover prudently incurred costs, and utilities must be presumed to act prudently. Ms. Alexander's proposal pays no heed to either legal principle. Her regime contemplates levying penalties for lower SQI results, irrespective of whether those results are the product of some action or inaction on the part of the utility. Levying penalties in circumstances where the utility has acted prudently is unjust and unreasonable. It would violate the fair return standard because the penalties would come straight out of the utility's earnings.

286. This issue has practical importance because, as addressed above, volatility in service quality is to be expected for reasons beyond FortisBC's control. For example, FBC's Customer Satisfaction has been adversely affected by the implementation of the Residential Conservation Rate, which the Commission approved and is consistent with provincial policy. The number of instances of public contact with pipelines varies with the amount of economic activity. Service interruption can occur when a car collides with a transmission structure, or due to an issue on BC Hydro's system.[466] The list goes on.

287. Under the last FBC PBR plans, there were instances where FBC missed targets. Yet, there was never an instance when the Commission found that FBC had earned a financial incentive at the expense of service quality. In other words, the Commission recognized the distinction between not meeting an SQI benchmark and declines in service quality caused by specific actions of the utility. By contrast, Ms. Alexander's recommendations do not recognize that the natural volatility in service quality will result in performance either exceeding or not meeting the benchmark at a given point in time. Penalizing the utility for natural volatility is unfair and contrary to the purpose of incorporating SQIs in a PBR Plan.

[466] T5:1044, ll.14-17 (Chernikhowsky).

Ms. Alexander's Proposal is Contrary to Due Process Requirements Under UCA

288. The Commission would have no jurisdiction to implement Ms. Alexander's penalty regime in any event. Unlike courts, a statutory body like the Commission has no "inherent jurisdiction" to make orders. The Commission gets its jurisdiction exclusively from statute. The only authority in the UCA for the Commission to issue a penalty is found in sections 109.1 and 109.2. Ms. Alexander's proposal is at odds with that section in two key respects:

- ***Mandatory penalties:*** Ms. Alexander's proposal is for mandatory penalties when SQI benchmarks are not met.[467] However, the UCA imposes a requirement to hold a hearing before any penalty is levied.[468] In other words, the Commission cannot (as Ms. Alexander's proposal would require) prejudge particular circumstances; rather, it must first hold a hearing to consider all of the relevant circumstances (or, as Ms. Alexander prefers to characterize it, to hear the utility's "sob stories"). Those circumstances must include whether the utility has caused the decline in service quality through imprudent or intentional conduct.

- ***Arbitrary penalties:*** The UCA also stipulates the factors to be considered in determining the amount of a penalty.[469] Ms. Alexander's proposed penalty amounts are arbitrary, and disproportionately high. They are tied to revenues (significantly inflated revenues too, since she quantified the penalty considering revenues associated with the commodity itself). There is no consideration under Ms. Alexander's proposal of, for instance: (a) intent, (b) the tangible impact on customer service associated with the decline in the particular SQI, or (c) the gains that the Company obtained at the expense of service quality, (d) the

[467] The implications of this proposal are addressed, for instance, at T5:939, l.14-942, l.12 (Alexander) and T5:985, l.14-986, l.3 (Alexander).

[468] Section 109.1(1).

[469] Section 109.2(3).

utility's overall performance under other metrics, and (e) the trend in the performance of the specific metric.

289. It should come as no surprise that Ms. Alexander's approach is (in her words) "certainly not routinely done in a number of states, at all".[470] The materials appended to her Evidence suggest that even this is an understatement; they indicate that out of the 41 states that responded to the survey, only nine "account for service quality in performance-based on incentive ratemaking mechanisms".[471]

(d) FortisBC's Further Response to Commissioner Cote's Invitation

290. As discussed, customer concerns regarding the potential for FortisBC to suddenly begin sacrificing service quality for short-term benefit are not based on evidence. The history of FortisBC, operating in both PBR and cost of service regimes, demonstrates the Companies' commitment to maintaining service quality. FortisBC thus maintains that the proposed treatment of SQIs in the context of the entire PBR Plan is appropriate. In the event that the Commission considers that tacit acknowledgement of its statutory powers is insufficient and that it should spell out enforcement principles, the Commission must ensure that any principles articulated accord with the UCA. In particular, the Commission should have regard to the following considerations.

- First, due process requires that the Companies should have an opportunity to explain why a deviation from the targeted SQI has occurred, in a manner similar to FEI's 2004 PBR Plan[472] and FBC's 2007 PBR Plan.[473]

---

[470] T5:1012, ll.11-21 (Alexander).

[471] FEI Exhibit C2-10, Alexander Evidence, p.17 of presentation slides: "Seven states said "yes," they do account for service quality in performance-based or incentive ratemaking mechanisms, with no change from 2001: CO, ME, MA, MS, NY, ND, and OR. Two states that said "no" in 2001 said "yes" in 2004: IA and MN". Ms. Alexander has also not indicated in her evidence whether the states that use her model have backing legislation, which in FortisBC's submission would be an important distinction.

[472] *In the Matter of An Application by Terasen Gas Inc. (formerly known as BC Gas Utility Ltd.) for Approval of a Multi-Year Performance-Based Rate Plan to Set Rates for 2004-2008*, Commission Order G-51-03, July 29, 2003, Appendix A, page 3 of 47.

- Second, the Commission should only entertain the prospect of initiating a review if the Companies' performance falls outside of a reasonable band around the target. A band is necessary to recognize that some volatility is to be expected.

- Third, causation is important. The Companies should not be penalized in the event that they have not directly caused the service decline through some improper conduct. This is consistent with FBC's prior PBR plan in which the Commission stated that it would "take into account the reasons given by the Company on why certain performance targets were not met and why the Company should be entitled to an incentive payment".[474]

- Fourth, a longer-term average ought to be used to allow for an understanding of the degradation, if any, and whether it is temporary or of a more permanent nature. For example, a wildfire or other unexpected event might lead to a short term degradation of certain SQIs.[475]

- Fifth, the Commission should have regard to the overall results for the suite of SQIs, not just a single SQI in isolation.

- Sixth, the consequence of an adverse finding that FortisBC has caused a decline in service should generally be limited to foregoing a portion of earnings sharing equal to the benefit that the Companies' derived from the improper conduct. This ensures proportionality.

- Seventh, the Commission should still employ directional indicators where the results can be significantly influenced (beyond minor volatility) by factors outside the Companies' control. That includes CSI, SAIDI/SAIFI, and public contact with pipelines.

---

[473] *In the Matter of An Application by FortisBC Inc. for Approval of its F2006 Revenue Requirement Application and Establishment of a Multi-Year Performance Based Regulation Mechanism*, Commission Order No. G-58-06, May 19, 2006 (the "FBC 2007 PBR Plan"), Appendix 1, p.28.

[474] FBC 2007 PBR Plan, Appendix 1, pp.4, 28.

[475] Exhibit B2-8, BCUC-FEI/FBC IR 3.25.3.

- Eighth, SQIs for safety should also still be directional. As described above, the goal for AIFR is zero. The Companies also answer to a separate regulator dedicated to workplace safety.

291. The Companies presented the PBR Plan as a package. The design or use of any mechanism that would allow for liberal disallowance of the Companies' portion of earnings sharing will pose a significant asymmetrical risk to the Companies that was not contemplated in the original PBR Plan. This asymmetrical risk will be amplified by setting benchmarks based on existing (or higher) service levels. The Companies already operate at a high level of service quality. In such circumstances, the odds are much greater that service quality will come in below the benchmark than come in above it. That type of approach would necessitate consideration of changes to other aspects of the PBR Plan, such as a downward adjustment of the X-Factor to provide the Companies with greater prospects of earning a fair return under the PBR Plan.

D. CONCLUSION ON SQIs

292. The Commission should approach the issue of SQIs giving due consideration to the fact that the Companies have maintained high service levels under both PBR and cost of service regulation. The SQIs should be directed at maintaining service levels, not increasing them - particularly when customers and the Commission have never identified any issues with the current levels. The existing mechanisms under the UCA are appropriate for guarding against the theoretical risk of the Companies sacrificing service quality for short-term gains. Ms. Alexander's penalty proposals must be rejected. In the event that the Commission considers the proposed PBR Plan and the existing statutory mechanisms to be insufficient, and considers it necessary to incorporate a term into the PBR Plan that makes earnings sharing conditional upon maintaining service quality, the Commission should proceed with caution to ensure that the PBR Plan remains compliant with the UCA and fair to the Company as well as customers.

PART SIX: CONCLUSION

293. FortisBC's proposed PBR Plan represents a balanced package that is fair to both customers and the Companies. It will provide a just and reasonable basis for setting rates for the next five years, and should be approved.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.

Dated: April 25, 2014 ***[original signed by Matthew Ghikas]***

Matthew Ghikas
Counsel for FortisBC Inc. and FortisBC Energy Inc.

Dated: April 25, 2014 ***[original signed by Tariq Ahmed]***

Tariq Ahmed
Counsel for FortisBC Inc. and FortisBC Energy Inc.

AUTHORITY

ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board), 2006 SCC 4

City of Calgary *Appellant/Respondent on cross-appeal*

v.

ATCO Gas and Pipelines Ltd. *Respondent/ Appellant on cross-appeal*

and

Alberta Energy and Utilities Board, Ontario Energy Board, Enbridge Gas Distribution Inc. and Union Gas Limited *Interveners*

Ville de Calgary *Appelante/Intimée au pourvoi incident*

c.

ATCO Gas and Pipelines Ltd. *Intimée/ Appelante au pourvoi incident*

et

Alberta Energy and Utilities Board, Commission de l'énergie de l'Ontario, Enbridge Gas Distribution Inc. et Union Gas Limited *Intervenantes*

Indexed as: ATCO Gas and Pipelines Ltd. *v.* Alberta (Energy and Utilities Board)

Neutral citation: 2006 SCC 4.

File No.: 30247.

2005: May 11; 2006: February 9.

Present: McLachlin C.J. and Bastarache, Binnie, LeBel, Deschamps, Fish and Charron JJ.

Répertorié : ATCO Gas and Pipelines Ltd. *c.* Alberta (Energy and Utilities Board)

Référence neutre : 2006 CSC 4.

N^{o} du greffe : 30247.

2005 : 11 mai; 2006 : 9 février.

Présents : La juge en chef McLachlin et les juges Bastarache, Binnie, LeBel, Deschamps, Fish et Charron.

ON APPEAL FROM THE COURT OF APPEAL FOR ALBERTA

EN APPEL DE LA COUR D'APPEL DE L'ALBERTA

Administrative law — Boards and tribunals — Regulatory boards — Jurisdiction — Doctrine of jurisdiction by necessary implication — Natural gas public utility applying to Alberta Energy and Utilities Board to approve sale of buildings and land no longer required in supplying natural gas — Board approving sale subject to condition that portion of sale proceeds be allocated to ratepaying customers of utility — Whether Board had explicit or implicit jurisdiction to allocate proceeds of sale — If so, whether Board's decision to exercise discretion to protect public interest by allocating proceeds of utility asset sale to customers reasonable — Alberta Energy and Utilities Board Act, R.S.A. 2000, c. A-17, s. 15(3) — Public Utilities Board Act, R.S.A. 2000, c. P-45, s. 37 — Gas Utilities Act, R.S.A. 2000, c. G-5, s. 26(2).

Droit administratif — Organismes et tribunaux administratifs — Organismes de réglementation — Compétence — Doctrine de la compétence par déduction nécessaire — Demande présentée à l'Alberta Energy and Utilities Board par un service public de gaz naturel pour obtenir l'autorisation de vendre des bâtiments et un terrain ne servant plus à la fourniture de gaz naturel — Autorisation accordée à la condition qu'une partie du produit de la vente soit attribuée aux clients du service public — L'organisme avait-il le pouvoir exprès ou tacite d'attribuer le produit de la vente? — Dans l'affirmative, sa décision d'exercer son pouvoir discrétionnaire de protéger l'intérêt public en attribuant aux clients une partie du produit de la vente était-elle raisonnable? — Alberta Energy and Utilities Board Act, R.S.A. 2000, ch. A-17, art. 15(3) — Public Utilities Board Act, R.S.A. 2000, ch. P-45, art. 37 — Gas Utilities Act, R.S.A. 2000, ch. G-5, art. 26(2).

Administrative law — Judicial review — Standard of review — Alberta Energy and Utilities Board — Standard

Droit administratif — Contrôle judiciaire — Norme de contrôle — Alberta Energy and Utilities Board

of review applicable to Board's jurisdiction to allocate proceeds from sale of public utility assets to ratepayers — Standard of review applicable to Board's decision to exercise discretion to allocate proceeds of sale — Alberta Energy and Utilities Board Act, R.S.A. 2000, c. A-17, s. 15(3) — Public Utilities Board Act, R.S.A. 2000, c. P-45, s. 37 — Gas Utilities Act, R.S.A. 2000, c. G-5, s. 26(2).

ATCO is a public utility in Alberta which delivers natural gas. A division of ATCO filed an application with the Alberta Energy and Utilities Board for approval of the sale of buildings and land located in Calgary, as required by the *Gas Utilities Act* ("GUA"). According to ATCO, the property was no longer used or useful for the provision of utility services, and the sale would not cause any harm to ratepaying customers. ATCO requested that the Board approve the sale transaction, as well as the proposed disposition of the sale proceeds: to retire the remaining book value of the sold assets, to recover the disposition costs, and to recognize that the balance of the profits resulting from the sale should be paid to ATCO's shareholders. The customers' interests were represented by the City of Calgary, who opposed ATCO's position with respect to the disposition of the sale proceeds to shareholders.

Persuaded that customers would not be harmed by the sale, the Board approved the sale transaction on the basis that customers would not "be exposed to the risk of financial harm as a result of the Sale that could not be examined in a future proceeding". In a second decision, the Board determined the allocation of net sale proceeds. The Board held that it had the jurisdiction to approve a proposed disposition of sale proceeds subject to appropriate conditions to protect the public interest, pursuant to the powers granted to it under s. 15(3) of the *Alberta Energy and Utilities Board Act* ("AEUBA"). The Board applied a formula which recognizes profits realized when proceeds of sale exceed the original cost can be shared between customers and shareholders, and allocated a portion of the net gain on the sale to the ratepaying customers. The Alberta Court of Appeal set aside the Board's decision, referring the matter back to the Board to allocate the entire remainder of the proceeds to ATCO.

Held (McLachlin C.J. and Binnie and Fish JJ. dissenting): The appeal is dismissed and the cross-appeal is allowed.

Per Bastarache, LeBel, Deschamps and Charron JJ.: When the relevant factors of the pragmatic and functional approach are properly considered, the standard of

— Norme de contrôle applicable à la décision de l'organisme concernant son pouvoir d'attribuer aux clients le produit de la vente des biens d'un service public — Norme de contrôle applicable à la décision de l'organisme d'exercer son pouvoir discrétionnaire en attribuant le produit de la vente — Alberta Energy and Utilities Board Act, R.S.A. 2000, ch. A-17, art. 15(3) — Public Utilities Board Act, R.S.A. 2000, ch. P-45, art. 37 — Gas Utilities Act, R.S.A. 2000, ch. G-5, art. 26(2).

ATCO est un service public albertain de distribution de gaz naturel. L'une de ses filiales a demandé à l'Alberta Energy and Utilities Board (« Commission ») l'autorisation de vendre des bâtiments et un terrain situés à Calgary, comme l'exigeait la *Gas Utilities Act* (« GUA »). ATCO a indiqué que les biens n'étaient plus utilisés pour fournir un service public ni susceptibles de l'être et que leur vente ne causerait aucun préjudice aux clients. Elle a demandé à la Commission d'autoriser l'opération et l'affectation du produit de la vente au paiement de la valeur comptable et au recouvrement des frais d'aliénation, et de reconnaître le droit de ses actionnaires au profit net. La ville de Calgary a défendu les intérêts des clients, s'opposant à ce que le produit de la vente soit attribué aux actionnaires comme le préconisait ATCO.

Convaincue que la vente ne serait pas préjudiciable aux clients, la Commission l'a autorisée au motif que « la vente ne risquait pas de leur infliger un préjudice financier qui ne pourrait faire l'objet d'un examen dans le cadre d'une procédure ultérieure ». Dans une deuxième décision, elle a décidé de l'attribution du produit net de la vente. Elle a conclu qu'elle avait le pouvoir d'autoriser l'aliénation projetée en l'assortissant de conditions aptes à protéger l'intérêt public, suivant le par. 15(3) de l'*Alberta Energy and Utilities Board Act* (« AEUBA »). Elle a appliqué une formule reconnaissant que le profit réalisé lorsque le produit de la vente excède le coût historique peut être réparti entre les clients et les actionnaires et elle a attribué aux clients une partie du gain net tiré de la vente. La Cour d'appel de l'Alberta a annulé la décision et renvoyé l'affaire à la Commission en lui enjoignant d'attribuer à ATCO la totalité du produit net.

Arrêt (la juge en chef McLachlin et les juges Binnie et Fish sont dissidents) : Le pourvoi est rejeté et le pourvoi incident est accueilli.

Les juges Bastarache, LeBel, Deschamps et Charron : Compte tenu des facteurs pertinents de l'analyse pragmatique et fonctionnelle, la norme de contrôle

review applicable to the Board's decision on the issue of jurisdiction is correctness. Here, the Board did not have the jurisdiction to allocate the proceeds of the sale of the utility's asset. The Court of Appeal made no error of fact or law when it concluded that the Board acted beyond its jurisdiction by misapprehending its statutory and common law authority. However, the Court of Appeal erred when it did not go on to conclude that the Board has no jurisdiction to allocate any portion of the proceeds of sale of the property to ratepayers. [21-34]

The interpretation of the AEUBA, the *Public Utilities Board Act* ("PUBA") and the GUA can lead to only one conclusion: the Board does not have the prerogative to decide on the distribution of the net gain from the sale of assets of a utility. On their grammatical and ordinary meaning, s. 26(2) GUA, s. 15(3) AEUBA and s. 37 PUBA are silent as to the Board's power to deal with sale proceeds. Section 26(2) GUA conferred on the Board the power to approve a transaction without more. The intended meaning of the Board's power pursuant to s. 15(3) AEUBA to impose conditions on an order that the Board considers necessary in the public interest, as well as the general power in s. 37 PUBA, is lost when the provisions are read in isolation. They are, on their own, vague and open-ended. It would be absurd to allow the Board an unfettered discretion to attach any condition it wishes to any order it makes. While the concept of "public interest" is very wide and elastic, the Board cannot be given total discretion over its limitations. These seemingly broad powers must be interpreted within the entire context of the statutes which are meant to balance the need to protect consumers as well as the property rights retained by owners, as recognized in a free market economy. The context indicates that the limits of the Board's powers are grounded in its main function of fixing just and reasonable rates and in protecting the integrity and dependability of the supply system. [7] [41] [43] [46]

An examination of the historical background of public utilities regulation in Alberta generally, and the legislation in respect of the powers of the Alberta Energy and Utilities Board in particular, reveals that nowhere is there a mention of the authority for the Board to allocate proceeds from a sale or the discretion of the Board to interfere with ownership rights. Moreover, although the Board may seem to possess a variety of powers and functions, it is manifest from a reading of the AEUBA,

applicable à la décision de la Commission portant sur sa compétence est celle de la décision correcte. En l'espèce, la Commission n'avait pas le pouvoir d'attribuer le produit de la vente des biens de l'entreprise de services publics. La Cour d'appel n'a pas commis d'erreur de fait ou de droit lorsqu'elle a conclu que la Commission avait outrepassé sa compétence en se méprenant sur les pouvoirs que lui conféraient la loi et la common law. Cependant, elle a eu tort de ne pas conclure en outre que la Commission n'avait pas le pouvoir d'attribuer aux clients quelque partie du produit de la vente des biens. [21-34]

L'analyse de l'AEUBA, de la *Public Utilities Board Act* (« PUBA ») et de la GUA mène à une seule conclusion : la Commission n'a pas le pouvoir de décider de la répartition du gain net tiré de la vente d'un bien par un service public. Suivant le sens grammatical et ordinaire des mots qui y sont employés, le par. 26(2) de la GUA, le par. 15(3) de l'AEUBA et l'art. 37 de la PUBA sont silencieux en ce qui concerne le pouvoir de la Commission de décider du sort du produit de la vente. Le paragraphe 26(2) de la GUA lui conférait le pouvoir d'autoriser une opération, sans plus. La véritable portée du par. 15(3) de l'AEUBA, qui confère à la Commission le pouvoir d'assortir une ordonnance des conditions qu'elle juge nécessaires dans l'intérêt public, et celle de l'art. 37 de la PUBA, qui l'investit d'un pouvoir général, est occultée lorsque l'on considère isolément ces dispositions. En elles-mêmes, les dispositions sont vagues et sujettes à diverses interprétations. Il serait absurde d'accorder à la Commission le pouvoir discrétionnaire absolu d'assortir ses ordonnances des conditions de son choix. La notion d'« intérêt public » est très large et élastique, mais la Commission ne peut se voir accorder le pouvoir discrétionnaire absolu d'en circonscrire les limites. Son pouvoir apparemment vaste doit être interprété dans le contexte global des lois en cause, qui visent à protéger non seulement le consommateur, mais aussi le droit de propriété reconnu au propriétaire dans une économie de libre marché. Il appert du contexte que les limites du pouvoir de la Commission sont inhérentes à sa principale fonction qui consiste à fixer des tarifs justes et raisonnables et à préserver l'intégrité et la fiabilité du réseau d'alimentation. [7] [41] [43] [46]

Ni l'historique de la réglementation des services publics de l'Alberta en général ni les dispositions législatives conférant ses pouvoirs à l'Alberta Energy and Utilities Board en particulier ne font mention du pouvoir de la Commission d'attribuer le produit de la vente ou de son pouvoir discrétionnaire de porter atteinte au droit de propriété. Bien que la Commission puisse sembler posséder toute une gamme d'attributions et de fonctions, il ressort de l'AEUBA, de la PUBA et de la

the PUBA and the GUA that the principal function of the Board in respect of public utilities, is the determination of rates. Its power to supervise the finances of these companies and their operations, although wide, is in practice incidental to fixing rates. The goals of sustainability, equity and efficiency, which underlie the reasoning as to how rates are fixed, have resulted in an economic and social arrangement which ensures that all customers have access to the utility at a fair price — nothing more. The rates paid by customers do not incorporate acquiring ownership or control of the utility's assets. The object of the statutes is to protect both the customer and the investor, and the Board's responsibility is to maintain a tariff that enhances the economic benefits to consumers and investors of the utility. This well-balanced regulatory arrangement does not, however, cancel the private nature of the utility. The fact that the utility is given the opportunity to make a profit on its services and a fair return on its investment in its assets should not and cannot stop the utility from benefiting from the profits which follow the sale of assets. Neither is the utility protected from losses incurred from the sale of assets. The Board misdirected itself by confusing the interests of the customers in obtaining safe and efficient utility service with an interest in the underlying assets owned only by the utility. [54-69]

Not only is the power to allocate the proceeds of the sale absent from the explicit language of the legislation, but it cannot be implied from the statutory regime as necessarily incidental to the explicit powers. For the doctrine of jurisdiction by necessary implication to apply, there must be evidence that the exercise of that power is a practical necessity for the Board to accomplish the objects prescribed by the legislature, something which is absent in this case. Not only is the authority to attach a condition to allocate the proceeds of a sale to a particular party unnecessary for the Board to accomplish its role, but deciding otherwise would lead to the conclusion that broadly drawn powers, such as those found in the AEUBA, the GUA and the PUBA, can be interpreted so as to encroach on the economic freedom of the utility, depriving it of its rights. If the Alberta legislature wishes to confer on ratepayers the economic benefits resulting from the sale of utility assets, it can expressly provide for this in the legislation. [39] [77-80]

Notwithstanding the conclusion that the Board lacked jurisdiction, its decision to exercise its discretion to protect the public interest by allocating the sale proceeds as it did to ratepaying customers did not meet a reasonable standard. When it explicitly concluded

GUA que son principal mandat à l'égard des entreprises de services publics est l'établissement de tarifs. Son pouvoir de surveiller les finances et le fonctionnement de ces entreprises est certes vaste mais, en pratique, il est accessoire à sa fonction première. Les objectifs de viabilité, d'équité et d'efficacité, qui expliquent le mode de fixation des tarifs, sont à l'origine d'un arrangement économique et social qui garantit à tous les clients l'accès au service public à un prix raisonnable, sans plus. Le paiement du tarif par le client n'emporte pas l'acquisition d'un droit de propriété ou de possession sur les biens du service public. L'objet de la législation est de protéger le client et l'investisseur, et la Commission a pour mandat d'établir une tarification qui favorise les avantages financiers de l'un et de l'autre. Toutefois, ce subtil compromis ne supprime pas le caractère privé de l'entreprise. Le fait que l'on donne au service public la possibilité de tirer un profit de la prestation du service et de bénéficier d'un juste rendement de son actif ne peut ni ne devrait l'empêcher d'encaisser le bénéfice résultant de la vente d'un élément d'actif. Sans compter que l'entreprise n'est pas à l'abri de la perte pouvant en découler. La Commission s'est méprise en confondant le droit des clients à un service sûr et efficace avec le droit sur les biens affectés à la prestation de ce service et dont l'entreprise est l'unique propriétaire. [54-69]

Non seulement le pouvoir d'attribuer le produit de la vente n'est pas expressément prévu par la loi, mais on ne peut « déduire » du régime législatif qu'il découle nécessairement du pouvoir exprès. Pour que s'applique la doctrine de la compétence par déduction nécessaire, la preuve doit établir que l'exercice de ce pouvoir est nécessaire dans les faits à la Commission pour que soient atteints les objectifs de la loi, ce qui n'est pas le cas en l'espèce. Non seulement il n'est pas nécessaire, pour s'acquitter de sa mission, que la Commission ait le pouvoir d'attribuer à une partie le produit de la vente qu'elle autorise, mais toute conclusion contraire permettrait d'interpréter un pouvoir largement défini, comme celui prévu dans l'AEUBA, la GUA ou la PUBA, d'une façon qui empiète sur la liberté économique de l'entreprise de services publics, dépouillant cette dernière de ses droits. Si l'assemblée législative albertaine souhaite que les clients bénéficient des avantages financiers découlant de la vente des biens d'un service public, elle peut adopter une disposition le prévoyant expressément. [39] [77-80]

Indépendamment de la conclusion que la Commission n'avait pas compétence, la décision d'exercer le pouvoir discrétionnaire de protéger l'intérêt public en répartissant le produit de la vente comme elle l'a fait ne satisfaisait pas à la norme de la raisonnabilité. Lorsqu'elle

that no harm would ensue to customers from the sale of the asset, the Board did not identify any public interest which required protection and there was, therefore, nothing to trigger the exercise of the discretion to allocate the proceeds of sale. Finally, it cannot be concluded that the Board's allocation was reasonable when it wrongly assumed that ratepayers had acquired a proprietary interest in the utility's assets because assets were a factor in the rate-setting process. [82-85]

Per McLachlin C.J. and Binnie and Fish JJ. (dissenting): The Board's decision should be restored. Section 15(3) AEUBA authorized the Board, in dealing with ATCO's application to approve the sale of the subject land and buildings, to "impose any additional conditions that the Board considers necessary in the public interest". In the exercise of that authority, and having regard to the Board's "general supervision over all gas utilities, and the owners of them" pursuant to s. 22(1) GUA, the Board made an allocation of the net gain for public policy reasons. The Board's discretion is not unlimited and must be exercised in good faith for its intended purpose. Here, in allocating one third of the net gain to ATCO and two thirds to the rate base, the Board explained that it was proper to balance the interests of both shareholders and ratepayers. In the Board's view to award the entire gain to the ratepayers would deny the utility an incentive to increase its efficiency and reduce its costs, but on the other hand to award the entire gain to the utility might encourage speculation in non-depreciable property or motivate the utility to identify and dispose of properties which have appreciated for reasons other than the best interest of the regulated business. Although it was open to the Board to allow ATCO's application for the entire profit, the solution it adopted in this case is well within the range of reasonable options. The "public interest" is largely and inherently a matter of opinion and discretion. While the statutory framework of utilities regulation varies from jurisdiction to jurisdiction, Alberta's grant of authority to its Board is more generous than most. The Court should not substitute its own view of what is "necessary in the public interest". The Board's decision made in the exercise of its jurisdiction was within the range of established regulatory opinion, whether the proper standard of review in that regard is patent unreasonableness or simple reasonableness. [91-92] [98-99] [110] [113] [122] [148]

a conclu explicitement que la vente des biens ne causerait aucun préjudice aux clients, la Commission n'a pas cerné d'intérêt public à protéger et aucun élément ne justifiait donc l'exercice de son pouvoir discrétionnaire d'attribuer le produit de la vente. Enfin, on ne peut conclure que la répartition était raisonnable, la Commission ayant supposé à tort que les clients avaient acquis un droit de propriété sur les biens de l'entreprise du fait de la prise en compte de ceux-ci dans l'établissement des tarifs. [82-85]

La juge en chef McLachlin et les juges Binnie et Fish (dissidents) : La décision de la Commission devrait être rétablie. Le paragraphe 15(3) de l'AEUBA conférait à la Commission le pouvoir d'« imposer les conditions supplémentaires qu'elle juge[ait] nécessaires dans l'intérêt public » en statuant sur la demande d'autorisation de vendre le terrain et les bâtiments en cause présentée par ATCO. Dans l'exercice de ce pouvoir, et vu la « surveillance générale des services de gaz et de leurs propriétaires » qui lui incombait suivant le par. 22(1) de la GUA, la Commission a réparti le gain net en se fondant sur des considérations d'intérêt public. Son pouvoir discrétionnaire n'est pas illimité et elle doit l'exercer de bonne foi et aux fins auxquelles il est conféré. Dans la présente affaire, en attribuant un tiers du gain net à ATCO et deux tiers à la base tarifaire, la Commission a expliqué qu'il fallait mettre en balance les intérêts des actionnaires et ceux des clients. Selon elle, attribuer aux clients la totalité du profit n'aurait pas incité l'entreprise à accroître son efficacité et à réduire ses coûts et l'attribuer à l'entreprise aurait pu encourager la spéculation à l'égard de biens non amortissables ou l'identification des biens dont la valeur s'était accrue et leur aliénation pour des motifs étrangers à l'intérêt véritable de l'entreprise réglementée. La Commission pouvait accueillir la demande d'ATCO et lui attribuer la totalité du profit, mais la solution qu'elle a retenue en l'espèce s'inscrivait parmi celles pour lesquelles elle pouvait raisonnablement opter. L'« intérêt public » tient essentiellement et intrinsèquement à l'opinion et au pouvoir discrétionnaire. Même si le cadre législatif de la réglementation des services publics varie d'un ressort à l'autre, la Commission s'est vu conférer par le législateur albertain un pouvoir plus étendu que celui accordé à la plupart des organismes apparentés. Il n'appartient pas à notre Cour de déterminer quelles conditions sont « nécessaires dans l'intérêt public » et de substituer son opinion à celle de la Commission. La décision que la Commission a rendue dans l'exercice de son pouvoir se situe dans les limites des opinions exprimées par les organismes de réglementation, que la norme applicable soit celle du manifestement déraisonnable ou celle du raisonnable simpliciter. [91-92] [98-99] [110] [113] [122] [148]

ATCO's submission that an allocation of profit to the customers would amount to a confiscation of the corporation's property overlooks the obvious difference between investment in an unregulated business and investment in a regulated utility where the ratepayers carry the costs and the regulator sets the return on investment, not the marketplace. The Board's response cannot be considered "confiscatory" in any proper use of the term, and is well within the range of what is regarded in comparable jurisdictions as an appropriate regulatory allocation of the gain on sale of land whose original investment has been included by the utility itself in its rate base. Similarly, ATCO's argument that the Board engaged in impermissible retroactive rate making should not be accepted. The Board proposed to apply a portion of the expected profit to future rate making. The effect of the order is prospective not retroactive. Fixing the going-forward rate of return, as well as general supervision of "all gas utilities, and the owners of them", were matters squarely within the Board's statutory mandate. ATCO also submits in its cross-appeal that the Court of Appeal erred in drawing a distinction between gains on sale of land whose original cost is not depreciated and depreciated property, such as buildings. A review of regulatory practice shows that many, but not all, regulators reject the relevance of this distinction. The point is not that the regulator must reject any such distinction but, rather, that the distinction does not have the controlling weight as contended by ATCO. In Alberta, it is up to the Board to determine what allocations are necessary in the public interest as conditions of the approval of sale. Finally, ATCO's contention that it alone is burdened with the risk on land that declines in value overlooks the fact that in a falling market the utility continues to be entitled to a rate of return on its original investment, even if the market value at the time is substantially less than its original investment. Further, it seems such losses are taken into account in the ongoing rate-setting process. [93] [123-147]

Cases Cited

By Bastarache J.

Referred to: *Re ATCO Gas-North*, Alta. E.U.B., Decision 2001-65, July 31, 2001; *TransAlta Utilities Corp. v. Public Utilities Board (Alta.)* (1986), 68 A.R. 171; *Re TransAlta Utilities Corp.*, Alta. E.U.B., Decision 2000-41, July 5, 2000; *Pushpanathan v.*

La prétention d'ATCO selon laquelle attribuer le profit aux clients équivaut à confisquer l'actif de l'entreprise ne tient pas compte de la différence manifeste entre un investissement dans une entreprise non réglementée et un investissement dans un service public réglementé; dans ce dernier cas, les clients supportent les coûts et le taux de rendement est fixé par un organisme de réglementation, et non par le marché. La mesure retenue par la Commission ne peut être qualifiée de « confiscatoire » dans quelque acception de ce terme et elle fait partie des solutions jugées acceptables dans des ressorts comparables en ce qui concerne l'attribution du profit tiré de la vente d'un terrain dont l'entreprise de services publics a elle-même inclus le coût historique dans sa base tarifaire. On ne peut non plus faire droit à la prétention d'ATCO voulant que la Commission se soit indûment livrée à une tarification rétroactive. La Commission a proposé de tenir compte d'une partie du profit escompté pour fixer les tarifs ultérieurs. L'ordonnance a un effet prospectif, et non rétroactif. La fixation du rendement futur et la surveillance générale « des services de gaz et de leurs propriétaires » relevaient sans conteste du mandat légal de la Commission. Dans son pourvoi incident, ATCO prétend en outre que la Cour d'appel de l'Alberta a établi à tort une distinction entre le profit tiré de la vente d'un terrain dont le coût historique n'est pas amorti et le profit tiré de la vente d'un bien amorti, comme un bâtiment. Il ressort de la pratique réglementaire que de nombreux organismes de réglementation, mais pas tous, jugent cette distinction non pertinente. Ce n'est pas que l'organisme de réglementation doive l'écarter systématiquement, mais elle n'est pas aussi déterminante que le prétend ATCO. En Alberta, la Commission peut autoriser une vente à la condition que le produit qui en est tiré soit réparti comme elle le juge nécessaire dans l'intérêt public. Enfin, la prétention selon laquelle ATCO assume seule le risque que la valeur d'un terrain diminue ne tient pas compte du fait que s'il y a contraction du marché, l'entreprise de services publics continue de bénéficier d'un rendement fondé sur le coût historique même si la valeur marchande a considérablement diminué. De plus, il appert qu'une telle perte est prise en considération dans la procédure d'établissement des tarifs. [93] [123-147]

Jurisprudence

Citée par le juge Bastarache

Arrêts mentionnés : *Re ATCO Gas-North*, Alta. E.U.B., Décision 2001-65, 31 juillet 2001; *TransAlta Utilities Corp. c. Public Utilities Board (Alta.)* (1986), 68 A.R. 171; *Re TransAlta Utilities Corp.*, Alta. E.U.B., Décision 2000-41, 5 juillet 2000; *Pushpanathan c.*

Canada (Minister of Citizenship and Immigration), [1998] 1 S.C.R. 982; *United Taxi Drivers' Fellowship of Southern Alberta v. Calgary (City)*, [2004] 1 S.C.R. 485, 2004 SCC 19; *Consumers' Gas Co. v. Ontario (Energy Board)*, [2001] O.J. No. 5024 (QL); *Coalition of Citizens Impacted by the Caroline Shell Plant v. Alberta (Energy Utilities Board)* (1996), 41 Alta. L.R. (3d) 374; *Atco Ltd. v. Calgary Power Ltd.*, [1982] 2 S.C.R. 557; *Dome Petroleum Ltd. v. Public Utilities Board (Alberta)* (1976), 2 A.R. 453, aff'd [1977] 2 S.C.R. 822; *Barrie Public Utilities v. Canadian Cable Television Assn.*, [2003] 1 S.C.R. 476, 2003 SCC 28; *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27; *Bell ExpressVu Limited Partnership v. Rex*, [2002] 2 S.C.R. 559, 2002 SCC 42; *H.L. v. Canada (Attorney General)*, [2005] 1 S.C.R. 401, 2005 SCC 25; *Marche v. Halifax Insurance Co.*, [2005] 1 S.C.R. 47, 2005 SCC 6; *Contino v. Leonelli-Contino*, [2005] 3 S.C.R. 217, 2005 SCC 63; *Re Alberta Government Telephones*, Alta. P.U.B., Decision No. E84081, June 29, 1984; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84116, October 12, 1984; *TransAlta Utilities Corp. (Re)*, [2002] A.E.U.B.D. No. 30 (QL); *ATCO Electric Ltd. (Re)*, [2003] A.E.U.B.D. No. 92 (QL); *Canadian Pacific Air Lines Ltd. v. Canadian Air Line Pilots Assn.*, [1993] 3 S.C.R. 724; *Bristol-Myers Squibb Co. v. Canada (Attorney General)*, [2005] 1 S.C.R. 533, 2005 SCC 26; *Chieu v. Canada (Minister of Citizenship and Immigration)*, [2002] 1 S.C.R. 84, 2002 SCC 3; *Bell Canada v. Canada (Canadian Radio-Television and Telecommunications Commission)*, [1989] 1 S.C.R. 1722; *R. v. McIntosh*, [1995] 1 S.C.R. 686; *Re Dow Chemical Canada Inc. and Union Gas Ltd.* (1982), 141 D.L.R. (3d) 641, aff'd (1983), 42 O.R. (2d) 731; *Interprovincial Pipe Line Ltd. v. National Energy Board*, [1978] 1 F.C. 601; *Canadian Broadcasting League v. Canadian Radio-television and Telecommunications Commission*, [1983] 1 F.C. 182, aff'd [1985] 1 S.C.R. 174; *Northwestern Utilities Ltd. v. City of Edmonton*, [1929] S.C.R. 186; *Northwestern Utilities Ltd. v. City of Edmonton*, [1979] 1 S.C.R. 684; *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Decision No. E84113, October 12, 1984; *Re Union Gas Ltd. and Ontario Energy Board* (1983), 1 D.L.R. (4th) 698; *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989); *Market St. Ry. Co. v. Railroad Commission of State of California*, 324 U.S. 548 (1945); *Re Coseka Resources Ltd. and Saratoga Processing Co.* (1981), 126 D.L.R. (3d) 705, leave to appeal refused, [1981] 2 S.C.R. vii; *Re Consumers' Gas Co.*, E.B.R.O. 410-II, 411-II, 412-II, March 23, 1987; *National Energy Board Act (Can.) (Re)*, [1986] 3 F.C. 275; *Pacific National Investments Ltd. v. Victoria (City)*, [2000] 2 S.C.R. 919, 2000 SCC 64; *Leiriao v. Val-Bélair (Town)*, [1991] 3 S.C.R. 349;

Canada (Ministre de la Citoyenneté et de l'Immigration), [1998] 1 R.C.S. 982; *United Taxi Drivers' Fellowship of Southern Alberta c. Calgary (Ville)*, [2004] 1 R.C.S. 485, 2004 CSC 19; *Consumers' Gas Co. c. Ontario (Energy Board)*, [2001] O.J. No. 5024 (QL); *Coalition of Citizens Impacted by the Caroline Shell Plant c. Alberta (Energy Utilities Board)* (1996), 41 Alta. L.R. (3d) 374; *Atco Ltd. c. Calgary Power Ltd.*, [1982] 2 R.C.S. 557; *Dome Petroleum Ltd. c. Public Utilities Board (Alberta)* (1976), 2 A.R. 453, conf. par [1977] 2 R.C.S. 822; *Barrie Public Utilities c. Assoc. canadienne de télévision par câble*, [2003] 1 R.C.S. 476, 2003 CSC 28; *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 R.C.S. 27; *Bell ExpressVu Limited Partnership c. Rex*, [2002] 2 R.C.S. 559, 2002 CSC 42; *H.L. c. Canada (Procureur général)*, [2005] 1 R.C.S. 401, 2005 CSC 25; *Marche c. Cie d'Assurance Halifax*, [2005] 1 R.C.S. 47, 2005 CSC 6; *Contino c. Leonelli-Contino*, [2005] 3 R.C.S. 217, 2005 CSC 63; *Re Alberta Government Telephones*, Alta. P.U.B., Décision nº E84081, 29 juin 1984; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision nº E84116, 12 octobre 1984; *TransAlta Utilities Corp. (Re)*, [2002] A.E.U.B.D. No. 30 (QL); *ATCO Electric Ltd. (Re)*, [2003] A.E.U.B.D. No. 92 (QL); *Lignes aériennes Canadien Pacifique Ltée c. Assoc. canadienne des pilotes de lignes aériennes*, [1993] 3 R.C.S. 724; *Bristol-Myers Squibb Co. c. Canada (Procureur général)*, [2005] 1 R.C.S. 533, 2005 CSC 26; *Chieu c. Canada (Ministre de la Citoyenneté et de l'Immigration)*, [2002] 1 R.C.S. 84, 2002 CSC 3; *Bell Canada c. Canada (Conseil de la radiodiffusion et des télécommunications canadiennes)*, [1989] 1 R.C.S. 1722; *R. c. McIntosh*, [1995] 1 R.C.S. 686; *Re Dow Chemical Canada Inc. and Union Gas Ltd.* (1982), 141 D.L.R. (3d) 641, conf. par (1983), 42 O.R. (2d) 731; *Interprovincial Pipe Line Ltd. c. Office national de l'énergie*, [1978] 1 C.F. 601; *Ligue de la radiodiffusion canadienne c. Conseil de la radiodiffusion et des télécommunications canadiennes*, [1983] 1 C.F. 182, conf. par [1985] 1 R.C.S. 174; *Northwestern Utilities Ltd. c. City of Edmonton*, [1929] R.C.S. 186; *Northwestern Utilities Ltd. c. Ville d'Edmonton*, [1979] 1 R.C.S. 684; *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Décision nº E84113, 12 octobre 1984; *Re Union Gas Ltd. and Ontario Energy Board* (1983), 1 D.L.R. (4th) 698; *Duquesne Light Co. c. Barasch*, 488 U.S. 299 (1989); *Market St. Ry. Co. c. Railroad Commission of State of California*, 324 U.S. 548 (1945); *Re Coseka Resources Ltd. and Saratoga Processing Co.* (1981), 126 D.L.R. (3d) 705, autorisation de pourvoi refusée, [1981] 2 R.C.S. vii; *Re Consumers' Gas Co.*, E.B.R.O. 410-II, 411-II, 412-II, 23 mars 1987; *Loi sur l'Office national de l'énergie (Can.) (Re)*, [1986] 3 C.F. 275; *Pacific National Investments Ltd. c. Victoria (Ville)*, [2000] 2

Hongkong Bank of Canada v. Wheeler Holdings Ltd., [1993] 1 S.C.R. 167.

By Binnie J. (dissenting)

Atco Ltd. v. Calgary Power Ltd., [1982] 2 S.C.R. 557; *C.U.P.E. v. Ontario (Minister of Labour)*, [2003] 1 S.C.R. 539, 2003 SCC 29; *TransAlta Utilities Corp. v. Public Utilities Board (Alta.)* (1986), 68 A.R. 171; *Dr. Q v. College of Physicians and Surgeons of British Columbia*, [2003] 1 S.C.R. 226, 2003 SCC 19; *Calgary Power Ltd. v. Copithorne*, [1959] S.C.R. 24; *United Brotherhood of Carpenters and Joiners of America, Local 579 v. Bradco Construction Ltd.*, [1993] 2 S.C.R. 316; *Pezim v. British Columbia (Superintendent of Brokers)*, [1994] 2 S.C.R. 557; *Memorial Gardens Association (Canada) Ltd. v. Colwood Cemetery Co.*, [1958] S.C.R. 353; *Union Gas Co. of Canada Ltd. v. Sydenham Gas and Petroleum Co.*, [1957] S.C.R. 185; *Re C.T.C. Dealer Holdings Ltd. and Ontario Securities Commission* (1987), 59 O.R. (2d) 79; *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, [2001] 2 S.C.R. 132, 2001 SCC 37; *Re Consumers' Gas Co.*, E.B.R.O. 341-I, June 30, 1976; *Re Boston Gas Co.*, 49 P.U.R. 4th 1 (1982); *Re Consumers' Gas Co.*, E.B.R.O. 465, March 1, 1991; *Re Natural Resource Gas Ltd.*, O.E.B., RP-2002-0147, EB-2002-0446, June 27, 2003; *Yukon Energy Corp. v. Utilities Board* (1996), 74 B.C.A.C. 58; *Re Arizona Public Service Co.*, 91 P.U.R. 4th 337 (1988); *Re Southern California Water Co.*, 43 C.P.U.C. 2d 596 (1992); *Re Southern California Gas Co.*, 118 P.U.R. 4th 81 (1990); *Democratic Central Committee of the District of Columbia v. Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (1973); *Board of Public Utility Commissioners v. New York Telephone Co.*, 271 U.S. 23 (1976); *Northwestern Utilities Ltd. v. City of Edmonton*, [1979] 1 S.C.R. 684; *New York Water Service Corp. v. Public Service Commission*, 208 N.Y.S.2d 857 (1960); *Re Compliance with the Energy Policy Act of 1992*, 62 C.P.U.C. 2d 517 (1995); *Re California Water Service Co.*, 66 C.P.U.C. 2d 100 (1996); *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84116, October 12, 1984; *Re Alberta Government Telephones*, Alta. P.U.B., Decision No. E84081, June 29, 1984; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84115, October 12, 1984; *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Decision No. E84113, October 12, 1984.

Statutes and Regulations Cited

Alberta Energy and Utilities Board Act, R.S.A. 2000, c. A-17, ss. 13, 15, 26(1), (2), 27.

R.C.S. 919, 2000 CSC 64; *Leiriao c. Val-Bélair (Ville)*, [1991] 3 R.C.S. 349; *Banque Hongkong du Canada c. Wheeler Holdings Ltd.*, [1993] 1 R.C.S. 167.

Citée par le juge Binnie (dissident)

Atco Ltd. c. Calgary Power Ltd., [1982] 2 R.C.S. 557; *S.C.F.P. c. Ontario (Ministre du Travail)*, [2003] 1 R.C.S. 539, 2003 CSC 29; *TransAlta Utilities Corp. c. Public Utilities Board (Alta.)* (1986), 68 A.R. 171; *Dr Q c. College of Physicians and Surgeons of British Columbia*, [2003] 1 R.C.S. 226, 2003 CSC 19; *Calgary Power Ltd. c. Copithorne*, [1959] R.C.S. 24; *Fraternité unie des charpentiers et menuisiers d'Amérique, section locale 579 c. Bradco Construction Ltd.*, [1993] 2 R.C.S. 316; *Pezim c. Colombie-Britannique (Superintendent of Brokers)*, [1994] 2 R.C.S. 557; *Memorial Gardens Association (Canada) Ltd. c. Colwood Cemetery Co.*, [1958] R.C.S. 353; *Union Gas Co. of Canada Ltd. c. Sydenham Gas and Petroleum Co.*, [1957] R.C.S. 185; *Re C.T.C. Dealer Holdings Ltd. and Ontario Securities Commission* (1987), 59 O.R. (2d) 79; *Comité pour le traitement égal des actionnaires minoritaires de la Société Asbestos ltée c. Ontario (Commission des valeurs mobilières)*, [2001] 2 R.C.S. 132, 2001 CSC 37; *Re Consumers' Gas Co.*, E.B.R.O. 341-I, 30 juin 1976; *Re Boston Gas Co.*, 49 P.U.R. 4th 1 (1982); *Re Consumers' Gas Co.*, E.B.R.O. 465, 1er mars 1991; *Re Natural Resource Gas Ltd.*, C.É.O., RP-2002-0147, EB-2002-0446, 27 juin 2003; *Yukon Energy Corp. c. Utilities Board* (1996), 74 B.C.A.C. 58; *Re Arizona Public Service Co.*, 91 P.U.R. 4th 337 (1988); *Re Southern California Water Co.*, 43 C.P.U.C. 2d 596 (1992); *Re Southern California Gas Co.*, 118 P.U.R. 4th 81 (1990); *Democratic Central Committee of the District of Columbia c. Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (1973); *Board of Public Utility Commissioners c. New York Telephone Co.*, 271 U.S. 23 (1976); *Northwestern Utilities Ltd. c. Ville d'Edmonton*, [1979] 1 R.C.S. 684; *New York Water Service Corp. c. Public Service Commission*, 208 N.Y.S.2d 857 (1960); *Re Compliance with the Energy Policy Act of 1992*, 62 C.P.U.C. 2d 517 (1995); *Re California Water Service Co.*, 66 C.P.U.C. 2d 100 (1996); *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision nº E84116, 12 octobre 1984; *Re Alberta Government Telephones*, Alta. P.U.B., Décision nº E84081, 29 juin 1984; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision nº E84115, 12 octobre 1984; *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Décision nº E84113, 12 octobre 1984.

Lois et règlements cités

Alberta Energy and Utilities Board Act, R.S.A. 2000, ch. A-17, art. 13, 15, 26(1), (2), 27.

Gas Utilities Act, R.S.A. 2000, c. G-5, ss. 16, 17, 22, 24, 26, 27(1), 36 to 45, 59.
Interpretation Act, R.S.A. 2000, c. I-8, s. 10.
Public Utilities Act, S.A. 1915, c. 6, ss. 21, 23, 24, 29(g).
Public Utilities Board Act, R.S.A. 2000, c. P-45, ss. 36, 37, 80, 85(1), 87, 89 to 95, 101(1), (2), 102(1).

Authors Cited

Anisman, Philip, and Robert F. Reid. *Administrative Law Issues and Practice*. Scarborough, Ont.: Carswell, 1995.

Black, Alexander J. "Responsible Regulation: Incentive Rates for Natural Gas Pipelines" (1992), 28 *Tulsa L.J.* 349.

Blake, Sara. *Administrative Law in Canada*, 3rd ed. Markham, Ont.: Butterworths, 2001.

Brown, David M. *Energy Regulation in Ontario*. Aurora, Ont.: Canada Law Book, 2001 (loose-leaf updated November 2004, release 3).

Brown, Donald J. M., and John M. Evans. *Judicial Review of Administrative Action in Canada*. Toronto: Canvasback, 1998 (loose-leaf updated July 2005).

Brown-John, C. Lloyd. *Canadian Regulatory Agencies: Quis custodiet ipsos custodes?* Toronto: Butterworths, 1981.

Canadian Institute of Resources Law. *Canada Energy Law Service: Alberta*. Edited by Steven A. Kennett. Toronto: Thomson Carswell, 1981 (loose-leaf updated 2005, release 2).

Côté, Pierre-André. *The Interpretation of Legislation in Canada*, 3rd ed. Scarborough, Ont.: Carswell, 2000.

Cross, Phillip S. "Rate Treatment of Gain on Sale of Land: Ratepayer Indifference, A New Standard?" (1990), 126 *Pub. Util. Fort.* 44.

Depoorter, Ben W. F. "Regulation of Natural Monopoly", in B. Bouckaert and G. De Geest, eds., *Encyclopedia of Law and Economics*, vol. III, *The Regulation of Contracts*. Northampton, Mass.: Edward Elgar, 2000.

Driedger, Elmer A. *Construction of Statutes*, 2nd ed. Toronto: Butterworths, 1983.

Green, Richard, and Martin Rodriguez Pardina. *Resetting Price Controls for Privatized Utilities: A Manual for Regulators*. Washington, D.C.: World Bank, 1999.

Kahn, Alfred E. *The Economics of Regulation: Principles and Institutions*, vol. 1, *Economic Principles*. Cambridge, Mass.: MIT Press, 1988.

MacAvoy, Paul W., and J. Gregory Sidak. "The Efficient Allocation of Proceeds from a Utility's Sale of Assets" (2001), 22 *Energy L.J.* 233.

Milner, H. R. "Public Utility Rate Control in Alberta" (1930), 8 *Can. Bar Rev.* 101.

Gas Utilities Act, R.S.A. 2000, ch. G-5, art. 16, 17, 22, 24, 26, 27(1), 36 à 45, 59.
Interpretation Act, R.S.A. 2000, ch. I-8, art. 10.
Public Utilities Act, S.A. 1915, ch. 6, art. 21, 23, 24, 29g).
Public Utilities Board Act, R.S.A. 2000, ch. P-45, art. 36, 37, 80, 85(1), 87, 89 à 95, 101(1), (2), 102(1).

Doctrine citée

Anisman, Philip, and Robert F. Reid. *Administrative Law Issues and Practice*. Scarborough, Ont. : Carswell, 1995.

Black, Alexander J. « Responsible Regulation : Incentive Rates for Natural Gas Pipelines » (1992), 28 *Tulsa L.J.* 349.

Blake, Sara. *Administrative Law in Canada*, 3rd ed. Markham, Ont. : Butterworths, 2001.

Brown, David M. *Energy Regulation in Ontario*. Aurora, Ont. : Canada Law Book, 2001 (loose-leaf updated November 2004, release 3).

Brown, Donald J. M., and John M. Evans. *Judicial Review of Administrative Action in Canada*. Toronto : Canvasback, 1998 (loose-leaf updated July 2005).

Brown-John, C. Lloyd. *Canadian Regulatory Agencies : Quis custodiet ipsos custodes?* Toronto : Butterworths, 1981.

Côté, Pierre-André. *Interprétation des lois*, 3e éd. Montréal : Thémis, 1999.

Cross, Phillip S. « Rate Treatment of Gain on Sale of Land: Ratepayer Indifference, A New Standard? » (1990), 126 *Pub. Util. Fort.* 44.

Depoorter, Ben W. F. « Regulation of Natural Monopoly », in B. Bouckaert and G. De Geest, eds., *Encyclopedia of Law and Economics*, vol. III, *The Regulation of Contracts*. Northampton, Mass. : Edward Elgar, 2000.

Driedger, Elmer A. *Construction of Statutes*, 2nd ed. Toronto : Butterworths, 1983.

Green, Richard, and Martin Rodriguez Pardina. *Resetting Price Controls for Privatized Utilities : A Manual for Regulators*. Washington, D.C. : World Bank, 1999.

Institut canadien du droit des ressources. *Canada Energy Law Service : Alberta*. Edited by Steven A. Kennett. Toronto : Thomson Carswell, 1981 (loose-leaf updated 2005, release 2).

Kahn, Alfred E. *The Economics of Regulation : Principles and Institutions*, vol. 1, *Economic Principles*. Cambridge, Mass. : MIT Press, 1988.

MacAvoy, Paul W., and J. Gregory Sidak. « The Efficient Allocation of Proceeds from a Utility's Sale of Assets » (2001), 22 *Energy L.J.* 233.

Mullan, David J. *Administrative Law.* Toronto: Irwin Law, 2001.

Netz, Janet S. "Price Regulation: A (Non-Technical) Overview", in B. Bouckaert and G. De Geest, eds., *Encyclopedia of Law and Economics*, vol. III, *The Regulation of Contracts.* Northampton, Mass.: Edward Elgar, 2000.

Reid, Robert F., and Hillel David. *Administrative Law and Practice*, 2nd ed. Toronto: Butterworths, 1978.

Sullivan, Ruth. *Sullivan and Driedger on the Construction of Statutes*, 4th ed. Markham, Ont.: Butterworths, 2002.

Trebilcock, Michael J. "The Consumer Interest and Regulatory Reform", in G. B. Doern, ed., *The Regulatory Process in Canada*. Toronto: Macmillan of Canada, 1978, 94.

APPEAL and CROSS-APPEAL from a judgment of the Alberta Court of Appeal (Wittmann J.A. and LoVecchio J. (*ad hoc*)) (2004), 24 Alta. L.R. (4th) 205, 339 A.R. 250, 312 W.A.C. 250, [2004] 4 W.W.R. 239, [2004] A.J. No. 45 (QL), 2004 ABCA 3, reversing a decision of the Alberta Energy and Utilities Board, [2002] A.E.U.B.D. No. 52 (QL). Appeal dismissed and cross-appeal allowed, McLachlin C.J. and Binnie and Fish JJ. dissenting.

Brian K. O'Ferrall and *Daron K. Naffin*, for the appellant/respondent on cross-appeal.

Clifton D. O'Brien, *Q.C.*, *Lawrence E. Smith*, *Q.C.*, *H. Martin Kay*, *Q.C.*, and *Laurie A. Goldbach*, for the respondent/appellant on cross-appeal.

J. Richard McKee and *Renée Marx*, for the intervener the Alberta Energy and Utilities Board.

Written submissions only by *George Vegh* and *Michael W. Lyle*, for the intervener the Ontario Energy Board.

Written submissions only by *J. L. McDougall*, *Q.C.*, and *Michael D. Schafler*, for the intervener Enbridge Gas Distribution Inc.

Written submissions only by *Michael A. Penny* and *Susan Kushneryk*, for the intervener Union Gas Limited.

Milner, H. R. « Public Utility Rate Control in Alberta » (1930), 8 *R. du B. can.* 101.

Mullan, David J. *Administrative Law.* Toronto : Irwin Law, 2001.

Netz, Janet S. « Price Regulation : A (Non-Technical) Overview », in B. Bouckaert and G. De Geest, eds., *Encyclopedia of Law and Economics*, vol. III, *The Regulation of Contracts.* Northampton, Mass. : Edward Elgar, 2000.

Reid, Robert F., and Hillel David. *Administrative Law and Practice*, 2nd ed. Toronto : Butterworths, 1978.

Sullivan, Ruth. *Sullivan and Driedger on the Construction of Statutes*, 4th ed. Markham, Ont. : Butterworths, 2002.

Trebilcock, Michael J. « The Consumer Interest and Regulatory Reform », in G. B. Doern, ed., *The Regulatory Process in Canada.* Toronto : Macmillan of Canada, 1978, 94.

POURVOI et POURVOI INCIDENT contre un arrêt de la Cour d'appel de l'Alberta (les juges Wittmann et LoVecchio (*ad hoc*)) (2004), 24 Alta. L.R. (4th) 205, 339 A.R. 250, 312 W.A.C. 250, [2004] 4 W.W.R. 239, [2004] A.J. No. 45 (QL), 2004 ABCA 3, qui a infirmé une décision de l'Alberta Energy and Utilities Board, [2002] A.E.U.B.D. No. 52 (QL). Pourvoi rejeté et pourvoi incident accueilli, la juge en chef McLachlin et les juges Binnie et Fish sont dissidents.

Brian K. O'Ferrall et *Daron K. Naffin*, pour l'appelante/intimée au pourvoi incident.

Clifton D. O'Brien, *c.r.*, *Lawrence E. Smith*, *c.r.*, *H. Martin Kay*, *c.r.*, et *Laurie A. Goldbach*, pour l'intimée/appelante au pourvoi incident.

J. Richard McKee et *Renée Marx*, pour l'intervenante Alberta Energy and Utilities Board.

Argumentation écrite seulement par *George Vegh* et *Michael W. Lyle*, pour l'intervenante la Commission de l'énergie de l'Ontario.

Argumentation écrite seulement par *J. L. McDougall*, *c.r.*, et *Michael D. Schafler*, pour l'intervenante Enbridge Gas Distribution Inc.

Argumentation écrite seulement par *Michael A. Penny* et *Susan Kushneryk*, pour l'intervenante Union Gas Limited.

The judgment of Bastarache, LeBel, Deschamps and Charron JJ. was delivered by

BASTARACHE J. —

1. Introduction

1 At the heart of this appeal is the issue of the jurisdiction of an administrative board. More specifically, the Court must consider whether, on the appropriate standard of review, this utility board appropriately set out the limits of its powers and discretion.

2 Few areas of our lives are now untouched by regulation. Telephone, rail, airline, trucking, foreign investment, insurance, capital markets, broadcasting licences and content, banking, food, drug and safety standards, are just a few of the objects of public regulations in Canada: M. J. Trebilcock, "The Consumer Interest and Regulatory Reform", in G. B. Doern, ed., *The Regulatory Process in Canada* (1978), 94. Discretion is central to the regulatory agency policy process, but this discretion will vary from one administrative body to another (see C. L. Brown-John, *Canadian Regulatory Agencies: Quis custodiet ipsos custodes?* (1981), at p. 29). More importantly, in exercising this discretion, statutory bodies must respect the confines of their jurisdiction: they cannot trespass in areas where the legislature has not assigned them authority (see D. J. Mullan, *Administrative Law* (2001), at pp. 9-10).

3 The business of energy and utilities is no exception to this regulatory framework. The respondent in this case is a public utility in Alberta which delivers natural gas. This public utility is nothing more than a private corporation subject to certain regulatory constraints. Fundamentally, it is like any other privately held company: it obtains the necessary funding from investors through public issues of shares in stock and bond markets; it is the

Version française du jugement des juges Bastarache, LeBel, Deschamps et Charron rendu par

LE JUGE BASTARACHE —

1. Introduction

Le présent pourvoi a pour objet la compétence d'un tribunal administratif. Plus précisément, notre Cour doit déterminer, selon la norme de contrôle appropriée, si l'organisme de réglementation a correctement circonscrit ses attributions et son pouvoir discrétionnaire.

De nos jours, rares sont les facettes de notre vie qui échappent à la réglementation. Le service téléphonique, les transports ferroviaire et aérien, le camionnage, l'investissement étranger, l'assurance, le marché des capitaux, la radiodiffusion (licences et contenu), les activités bancaires, les aliments, les médicaments et les normes de sécurité ne constituent que quelques-uns des objets de la réglementation au Canada : M. J. Trebilcock, « The Consumer Interest and Regulatory Reform », dans G. B. Doern, dir., *The Regulatory Process in Canada* (1978), 94. Le pouvoir discrétionnaire est au cœur de l'élaboration des politiques des organismes administratifs, mais son étendue varie d'un organisme à l'autre (voir C. L. Brown-John, *Canadian Regulatory Agencies : Quis custodiet ipsos custodes?* (1981), p. 29). Et, plus important encore, dans l'exercice de son pouvoir discrétionnaire, l'organisme créé par voie législative doit s'en tenir à son domaine de compétence : il ne peut s'immiscer dans un autre pour lequel le législateur ne lui a pas attribué compétence (voir D. J. Mullan, *Administrative Law* (2001), p. 9-10).

Le secteur de l'énergie et des services publics n'y échappe pas. En l'espèce, l'intimée est un service public albertain de distribution de gaz naturel. Il ne s'agit en fait que d'une société privée assujettie à certaines contraintes réglementaires. Essentiellement, elle est dans la même situation que toute société privée : elle obtient son financement par l'émission d'actions et d'obligations; ses ressources, ses terrains et ses autres biens lui

sole owner of the resources, land and other assets; it constructs plants, purchases equipment, and contracts with employees to provide the services; it realizes profits resulting from the application of the rates approved by the Alberta Energy and Utilities Board ("Board") (see P. W. MacAvoy and J. G. Sidak, "The Efficient Allocation of Proceeds from a Utility's Sale of Assets" (2001), 22 *Energy L.J.* 233, at p. 234). That said, one cannot ignore the important feature which makes a public utility so distinct: it must answer to a regulator. Public utilities are typically natural monopolies: technology and demand are such that fixed costs are lower for a single firm to supply the market than would be the case where there is duplication of services by different companies in a competitive environment (see A. E. Kahn, *The Economics of Regulation: Principles and Institutions* (1988), vol. 1, at p. 11; B. W. F. Depoorter, "Regulation of Natural Monopoly", in B. Bouckaert and G. De Geest, eds., *Encyclopedia of Law and Economics* (2000), vol. III, 498; J. S. Netz, "Price Regulation: A (Non-Technical) Overview", in B. Bouckaert and G. De Geest, eds., *Encyclopedia of Law and Economics* (2000), vol. III, 396, at p. 398; A. J. Black, "Responsible Regulation: Incentive Rates for Natural Gas Pipelines" (1992), 28 *Tulsa L.J.* 349, at p. 351). Efficiency of production is promoted under this model. However, governments have purported to move away from this theoretical concept and have adopted what can only be described as a "regulated monopoly". The utility regulations exist to protect the public from monopolistic behaviour and the consequent inelasticity of demand while ensuring the continued quality of an essential service (see Kahn, at p. 11).

As in any business venture, public utilities make business decisions, their ultimate goal being to maximize the residual benefits to shareholders. However, the regulator limits the utility's managerial discretion over key decisions, including prices, service offerings and the prudency of plant and equipment investment decisions. And more relevant to this case, the utility, outside the ordinary course of business, is limited in its right to sell

appartiennent en propre; elle construit des installations, achète du matériel et, pour fournir ses services, conclut des contrats avec des employés; elle réalise des profits en pratiquant des tarifs approuvés par l'Alberta Energy and Utilities Board (« Commission ») (voir P. W. MacAvoy et J. G. Sidak, « The Efficient Allocation of Proceeds from a Utility's Sale of Assets » (2001), 22 *Energy L.J.* 233, p. 234). Cela dit, on ne peut faire abstraction de la caractéristique importante qui rend un service public si distinct : il doit rendre compte à un organisme de réglementation. Les services publics sont habituellement des monopoles naturels : la technologie requise et la demande sont telles que les coûts fixes sont moindres lorsque le marché est desservi par une seule entreprise au lieu de plusieurs faisant double-emploi dans un contexte concurrentiel (voir A. E. Kahn, *The Economics of Regulation : Principles and Institutions* (1988), vol. 1, p. 11; B. W. F. Depoorter, « Regulation of Natural Monopoly », dans B. Bouckaert et G. De Geest, dir., *Encyclopedia of Law and Economics* (2000), vol. III, 498; J. S. Netz, « Price Regulation : A (Non-Technical) Overview », dans B. Bouckaert et G. De Geest, dir., *Encyclopedia of Law and Economics* (2000), vol. III, 396, p. 398; A. J. Black, « Responsible Regulation : Incentive Rates for Natural Gas Pipelines » (1992), 28 *Tulsa L.J.* 349, p. 351). Ce modèle favorise l'efficience de la production. Toutefois, les gouvernements ont voulu s'éloigner du concept théorique et ont opté pour ce qu'il convient d'appeler un « monopole réglementé ». La réglementation des services publics vise à protéger la population contre un comportement monopolistique et l'inélasticité de la demande qui en résulte tout en assurant la qualité constante d'un service essentiel (voir Kahn, p. 11).

Comme toute autre entreprise, un service public prend des décisions d'affaires, son objectif ultime étant de maximiser les profits revenant aux actionnaires. Cependant, l'organisme de réglementation restreint son pouvoir discrétionnaire à l'égard de certains éléments clés, dont les prix, les services offerts et l'opportunité d'investir dans des installations et du matériel. Et, plus important encore dans la présente affaire, il restreint également son

assets it owns: it must obtain authorization from its regulator before selling an asset previously used to produce regulated services (see MacAvoy and Sidak, at p. 234).

5 Against this backdrop, the Court is being asked to determine whether the Board has jurisdiction pursuant to its enabling statutes to allocate a portion of the net gain on the sale of a now discarded utility asset to the rate-paying customers of the utility when approving the sale. Subsequently, if this first question is answered affirmatively, the Court must consider whether the Board's exercise of its jurisdiction was reasonable and within the limits of its jurisdiction: was it allowed, in the circumstances of this case, to allocate a portion of the net gain on the sale of the utility to the rate-paying customers?

6 The customers' interests are represented in this case by the City of Calgary ("City") which argues that the Board can determine how to allocate the proceeds pursuant to its power to approve the sale and protect the public interest. I find this position unconvincing.

7 The interpretation of the *Alberta Energy and Utilities Board Act*, R.S.A. 2000, c. A-17 ("AEUBA"), the *Public Utilities Board Act*, R.S.A. 2000, c. P-45 ("PUBA"), and the *Gas Utilities Act*, R.S.A. 2000, c. G-5 ("GUA") (see Appendix for the relevant provisions of these three statutes), can lead to only one conclusion: the Board does not have the prerogative to decide on the distribution of the net gain from the sale of assets of a utility. The Board's seemingly broad powers to make any order and to impose any additional conditions that are necessary in the public interest has to be interpreted within the entire context of the statutes which are meant to balance the need to protect consumers as well as the property rights retained by owners, as recognized in a free market economy. The limits of the powers of the Board are grounded in its main function of fixing just and reasonable rates ("rate setting") and in protecting the integrity and dependability of the supply system.

pouvoir de vendre ses biens en dehors du cours normal de ses activités : son autorisation doit être obtenue pour la vente d'un bien affecté jusqu'alors à la prestation d'un service réglementé (voir MacAvoy et Sidak, p. 234).

C'est dans ce contexte qu'on demande à notre Cour de déterminer si, lorsqu'elle autorise un service public à vendre un bien désaffecté, la Commission peut, suivant ses lois habilitantes, attribuer aux clients une partie du gain net obtenu. Dans l'affirmative, il nous faut décider si la Commission a raisonnablement exercé son pouvoir et respecté les limites de sa compétence : était-elle autorisée, en l'espèce, à attribuer une partie du gain net aux clients?

La ville de Calgary (« Ville ») défend les intérêts des clients dans le cadre du présent pourvoi. Elle soutient que la Commission peut décider de l'attribution du produit de la vente en vertu de son pouvoir d'autoriser ou non l'opération et de protéger l'intérêt public. Cette thèse me paraît peu convaincante.

L'analyse de l'*Alberta Energy and Utilities Board Act*, R.S.A. 2000, ch. A-17 (« AEUBA »), de la *Public Utilities Board Act*, R.S.A. 2000, ch. P-45 (« PUBA »), et de la *Gas Utilities Act*, R.S.A. 2000, ch. G-5 (« GUA ») (voir leurs dispositions pertinentes en annexe) mène à une seule conclusion : la Commission n'a pas le pouvoir de décider de la répartition du gain net tiré de la vente d'un bien par un service public. Son pouvoir apparemment vaste de rendre toute décision et d'imposer les conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public doit être interprété dans le contexte global des lois en cause qui visent à protéger non seulement le consommateur, mais aussi le droit de propriété reconnu au propriétaire dans une économie de libre marché. Les limites du pouvoir de la Commission sont inhérentes à sa principale fonction qui consiste à fixer des tarifs justes et raisonnables (la tarification) et à préserver l'intégrité et la fiabilité du réseau d'alimentation.

1.1 *Overview of the Facts*

ATCO Gas - South ("AGS"), which is a division of ATCO Gas and Pipelines Ltd. ("ATCO"), filed an application by letter with the Board pursuant to s. 25.1(2) (now s. 26(2)) of the GUA, for approval of the sale of its properties located in Calgary known as Calgary Stores Block (the "property"). The property consisted of land and buildings; however, the main value was in the land, and the purchaser intended to and did eventually demolish the buildings and redevelop the land. According to AGS, the property was no longer used or useful for the provision of utility services, and the sale would not cause any harm to customers. In fact, AGS suggested that the sale would result in cost savings to customers, by allowing the net book value of the property to be retired and withdrawn from the rate base, thereby reducing rates. ATCO requested that the Board approve the sale transaction and the disposition of the sale proceeds to retire the remaining book value of the sold assets, to recover the disposition costs, and to recognize the balance of the profits resulting from the sale of the plant should be paid to shareholders. The Board dealt with the application in writing, without witnesses or an oral hearing. Other parties making written submissions to the Board were the City of Calgary, the Federation of Alberta Gas Co-ops Ltd., Gas Alberta Inc. and the Municipal Interveners, who all opposed ATCO's position with respect to the disposition of the sale proceeds to shareholders.

1.2 *Judicial History*

1.2.1 Alberta Energy and Utilities Board

1.2.1.1 *Decision 2001-78*

In a first decision, which considered ATCO's application to approve the sale of the property, the Board employed a "no-harm" test, assessing the potential impact on both rates and the level of service to customers and the prudence of the sale transaction, taking into account the purchaser and tender or sale process followed. The Board was of the view that the test had been satisfied. It was

1.1 *Aperçu des faits*

8 ATCO Gas - South (« AGS »), une filiale d'ATCO Gas and Pipelines Ltd. (« ATCO »), a fait parvenir à la Commission une lettre dans laquelle elle lui demandait, en application du par. 25.1(2) (l'actuel par. 26(2)) de la GUA, l'autorisation de vendre des biens situés à Calgary (le *Calgary Stores Block*). Ces biens étaient constitués d'un terrain et de bâtiments, mais c'est le terrain qui présentait le plus grand intérêt, et l'acquéreur comptait démolir les bâtiments et réaménager le terrain, ce qu'il a d'ailleurs fait. Devant la Commission, AGS a indiqué que les biens n'étaient plus utilisés pour fournir un service public ni susceptibles de l'être et que leur vente ne causerait aucun préjudice aux clients. AGS a en fait laissé entendre que l'opération se traduirait par une économie pour les clients du fait que la valeur comptable nette des biens ne serait plus prise en compte dans l'établissement de la base tarifaire, diminuant d'autant les tarifs. ATCO a demandé à la Commission d'autoriser l'opération et l'affectation du produit de la vente au paiement du solde de la valeur comptable et au recouvrement des frais d'aliénation, puis de permettre le versement du gain net aux actionnaires. La Commission a examiné la demande sur dossier sans entendre de témoins ni tenir d'audience. La Ville, Federation of Alberta Gas Co-ops Ltd., Gas Alberta Inc. et des intervenants municipaux ont déposé des observations écrites. Tous s'opposaient à ce que le produit de la vente soit attribué aux actionnaires comme le préconisait ATCO.

1.2 *Historique judiciaire*

1.2.1 La Commission

1.2.1.1 *Décision 2001-78*

9 Dans une première décision relative à la demande d'autorisation de la vente des biens, la Commission a appliqué le critère de l'« absence de préjudice » et soupesé les répercussions possibles sur les tarifs et la qualité des services offerts aux clients, ainsi que l'opportunité de l'opération, compte tenu de l'acquéreur et de la procédure d'appel d'offres ou de vente suivie. Elle a conclu à l'« absence de

persuaded that customers would not be harmed by the sale, given that a prudent lease arrangement to replace the sold facility had been concluded. The Board was satisfied that there would not be a negative impact on customers' rates, at least during the five-year initial term of the lease. In fact, the Board concluded that there would be cost savings to the customers and that there would be no impact on the level of service to customers as a result of the sale. It did not make a finding on the specific impact on future operating costs; for example, it did not consider the costs of the lease arrangement entered into by ATCO. The Board noted that those costs could be reviewed by the Board in a future general rate application brought by interested parties.

1.2.1.2 *Decision 2002-037, [2002] A.E.U.B.D. No. 52 (QL)*

10 In a second decision, the Board determined the allocation of net sale proceeds. It reviewed the regulatory policy and general principles which affected the decision, although no specific matters are enumerated for consideration in the applicable legislative provisions. The Board had previously developed a "no-harm" test, and it reviewed the rationale for the test as summarized in its Decision 2001-65 (*Re ATCO Gas-North*): "The Board considers that its power to mitigate or offset potential harm to customers by allocating part or all of the sale proceeds to them, flows from its very broad mandate to protect consumers in the public interest" (p. 16).

11 The Board went on to discuss the implications of the Alberta Court of Appeal decision in *TransAlta Utilities Corp. v. Public Utilities Board (Alta.)* (1986), 68 A.R. 171, referring to various decisions it had rendered in the past. Quoting from its Decision 2000-41 (*Re TransAlta Utilities Corp.*), the Board summarized the "*TransAlta Formula*":

> In subsequent decisions, the Board has interpreted the Court of Appeal's conclusion to mean that where the sale price exceeds the original cost of the assets, shareholders are entitled to net book value (in historical dollars), customers are entitled to the difference between

préjudice ». Elle s'est dite convaincue que la vente ne serait pas préjudiciable aux clients étant donné l'entente de location judicieusement conclue en vue du remplacement des installations vendues. Elle a estimé qu'il n'y aurait pas d'effet négatif sur les tarifs exigés des clients, du moins les cinq premières années de la location. La Commission a en fait jugé que la vente permettrait aux clients d'obtenir les mêmes services à meilleur prix. Elle ne s'est pas prononcée sur les effets de l'opération sur les frais d'exploitation futurs; à titre d'exemple, elle n'a pas tenu compte des frais liés à l'entente de location conclue par ATCO. La Commission a dit que les parties intéressées et elle pourraient se pencher sur ces frais dans le cadre d'une demande générale d'approbation de tarifs.

1.2.1.2 *Décision 2002-037, [2002] A.E.U.B.D. No. 52 (QL)*

Dans une deuxième décision, la Commission a décidé de l'attribution du produit net de la vente. Elle a fait état de la politique réglementaire et des principes généraux présidant à la décision, même si les dispositions législatives applicables n'énumèrent pas les facteurs précis devant être pris en compte. Elle a fait mention du critère de l'« absence de préjudice » élaboré auparavant et dont elle avait résumé la raison d'être dans sa décision 2001-65 (*Re ATCO Gas-North*) : [TRADUCTION] « La Commission estime que son pouvoir de limiter ou de compenser le préjudice que pourraient subir les clients en leur attribuant tout ou partie du produit de la vente découle de son vaste mandat de protéger les clients dans l'intérêt public » (p. 16).

La Commission a ensuite analysé les répercussions de l'arrêt *TransAlta Utilities Corp. c. Public Utilities Board (Alta.)* (1986), 68 A.R. 171, de la Cour d'appel de l'Alberta, en se référant à différentes décisions qu'elle avait rendues. Citant sa décision 2000-41 (*Re TransAlta Utilities Corp.*), voici comment elle a résumé la « *formule TransAlta* » :

> [TRADUCTION] Dans des décisions subséquentes, la Commission a conclu que pour la Cour d'appel, lorsque le prix de vente des biens est plus élevé que leur coût historique, les actionnaires ont droit à la valeur comptable nette (en fonction de la valeur historique),

net book value and original cost, and any appreciation in the value of the assets (i.e. the difference between original cost and the sale price) is to be shared by shareholders and customers. The amount to be shared by each is determined by multiplying the ratio of sale price/original cost to the net book value (for shareholders) and the difference between original cost and net book value (for customers). However, where the sale price does not exceed original cost, customers are entitled to all of the gain on sale. [para. 27]

les clients ont droit à la différence entre la valeur comptable nette et le coût historique, et toute appréciation des biens (c.-à-d. la différence entre le coût historique et le prix de vente) est répartie entre les actionnaires et les clients. Le montant attribué aux actionnaires est calculé en multipliant le ratio prix de vente/coût historique par la valeur comptable nette et celui qui revient aux clients est obtenu en multipliant ce ratio par la différence entre le coût historique et la valeur comptable nette. Toutefois, lorsque le prix de vente n'est pas supérieur au coût historique, les clients ont droit à la totalité du gain réalisé lors de la vente. [par. 27]

The Board also referred to Decision 2001-65, where it had clarified the following:

In the Board's view, if the TransAlta Formula yields a result greater than the no-harm amount, customers are entitled to the greater amount. If the TransAlta Formula yields a result less than the no-harm amount, customers are entitled to the no-harm amount. In the Board's view, this approach is consistent with its historical application of the TransAlta Formula. [para. 28]

La Commission a également cité la décision 2001-65 renfermant les explications suivantes :

[TRADUCTION] Selon la Commission, lorsque l'application de la formule TransAlta donne un montant supérieur à celui obtenu en appliquant le critère de l'absence de préjudice, les clients ont droit au montant plus élevé. Par contre, lorsqu'elle débouche sur un montant inférieur à celui obtenu en appliquant le critère de l'absence de préjudice, les clients ont droit à ce dernier montant. De plus, cette approche est compatible avec la manière dont elle a appliqué jusqu'à maintenant la formule TransAlta. [par. 28]

On the issue of its jurisdiction to allocate the net proceeds of a sale, the Board in the present case stated:

The fact that a regulated utility must seek Board approval before disposing of its assets is sufficient indication of the limitations placed by the legislature on the property rights of a utility. In appropriate circumstances, the Board clearly has the power to prevent a utility from disposing of its property. In the Board's view it also follows that the Board can approve a disposition subject to appropriate conditions to protect customer interests.

Regarding AGS's argument that allocating more than the no-harm amount to customers would amount to retrospective ratemaking, the Board again notes the decision in the TransAlta Appeal. The Court of Appeal accepted that the Board could include in the definition of "revenue" an amount payable to customers representing excess depreciation paid by them through past rates. In the Board's view, no question of retrospective ratemaking arises in cases where previously regulated rate base assets are being disposed of out of rate base and the Board applies the TransAlta Formula.

En ce qui concerne son pouvoir de répartir le produit net de la vente, la Commission a dit : 12

[TRADUCTION] Le fait qu'un service public réglementé doive obtenir de la Commission l'autorisation de se départir d'un bien montre que l'assemblée législative a voulu limiter son droit de propriété. Dans certaines circonstances, la Commission a clairement le pouvoir d'empêcher un service public de se départir d'un bien. Selon nous, il s'ensuit également que la Commission peut autoriser une aliénation en l'assortissant de conditions aptes à protéger les intérêts des clients.

Pour ce qui est de l'argument d'AGS selon lequel l'attribution aux clients d'un montant supérieur à celui obtenu en appliquant le critère de l'absence de préjudice équivaudrait à une tarification rétroactive, la Commission cite à nouveau l'arrêt *TransAlta* dans lequel la Cour d'appel a reconnu que la Commission pouvait assimiler à un « revenu » un montant payable aux clients pour les indemniser de l'amortissement excédentaire pris en compte dans la tarification antérieure. Il ne saurait y avoir de tarification rétroactive lorsqu'un service public se dessaisit d'un bien auparavant inclus dans la base tarifaire et que la Commission applique la formule TransAlta.

The Board is not persuaded by the Company's argument that the Stores Block assets are now 'non-utility' by virtue of being 'no longer required for utility service'. The Board notes that the assets could still be providing service to regulated customers. In fact, the services formerly provided by the Stores Block assets continue to be required, but will be provided from existing and newly leased facilities. Furthermore, the Board notes that even when an asset and the associated service it was providing to customers is no longer required the Board has previously allocated more than the no-harm amount to customers where proceeds have exceeded the original cost of the asset. [paras. 47-49]

L'argument de la société voulant que les biens (le *Calgary Stores Block*) ne soient plus des biens du service public parce qu'ils ne sont plus requis pour fournir le service ne nous convainc pas. La Commission signale que les biens pourraient encore servir à la prestation de services destinés aux clients de l'entreprise réglementée. En fait, les services anciennement fournis grâce aux biens demeurent requis, mais leur prestation sera assurée par des installations existantes et des installations récemment louées. La Commission note de plus que même dans le cas où un bien et le service qu'il fournissait aux clients ne sont plus requis, elle a déjà attribué plus que le montant obtenu par l'application du critère de l'absence de préjudice lorsque le produit de l'aliénation a été supérieur au coût historique. [par. 47-49]

13 The Board went on to apply the no-harm test to the present facts. It noted that in its decision on the application for the approval of the sale, it had already considered the no-harm test to be satisfied. However, in that first decision, it had not made a finding with respect to the specific impact on future operating costs, including the particular lease arrangement being entered into by ATCO.

La Commission a ensuite appliqué le critère de l'absence de préjudice aux faits de l'espèce. Elle a signalé que, dans sa décision relative à la demande d'autorisation, elle avait conclu au respect de ce critère, mais n'avait alors tiré aucune conclusion concernant l'incidence sur les frais d'exploitation, notamment l'entente de location obtenue par ATCO.

14 The Board then reviewed the submissions with respect to the allocation of the net gain and rejected the submission that if the new owner had no use of the buildings on the land, this should affect the allocation of net proceeds. The Board held that the buildings did have some present value but did not find it necessary to fix a specific value. The Board recognized and confirmed that the *TransAlta Formula* was one whereby the "windfall" realized when the proceeds of sale exceed the original cost could be shared between customers and shareholders. It held that it should apply the formula in this case and that it would consider the gain on the transaction as a whole, not distinguishing between the proceeds allocated to land separately from the proceeds allocated to buildings.

Puis, après avoir examiné les observations portant sur l'attribution du gain net, la Commission a rejeté l'argument selon lequel le fait que le nouveau propriétaire n'utiliserait pas les bâtiments situés sur le terrain était déterminant à cet égard. Elle a conclu que les bâtiments avaient alors une certaine valeur, mais elle n'a pas jugé nécessaire de la préciser. Elle a reconnu et confirmé que suivant la *formule TransAlta*, le profit inattendu réalisé lorsque le produit de la vente excède le coût historique pouvait être réparti entre les clients et les actionnaires. Elle a estimé qu'il y avait lieu en l'espèce d'appliquer la formule et de tenir compte de la totalité du gain issu de l'opération sans dissocier la partie attribuable au terrain et celle correspondant aux bâtiments.

15 With respect to allocation of the gain between customers and shareholders of ATCO, the Board tried to balance the interests of both the customers' desire for safe reliable service at a reasonable cost with the provision of a fair return on the investment made by the company:

Pour ce qui est de la répartition du gain entre les clients et les actionnaires d'ATCO, la Commission a tenté de mettre en balance la volonté des clients d'obtenir des services à la fois sûrs et fiables à un prix raisonnable et celle des investisseurs de toucher un rendement raisonnable :

To award the entire net gain on the land and buildings to the customers, while beneficial to the customers, could establish an environment that may deter the process wherein the company continually assesses its operation to identify, evaluate, and select options that continually increase efficiency and reduce costs.

Conversely, to award the entire net gain to the company may establish an environment where a regulated utility company might be moved to speculate in non-depreciable property or result in the company being motivated to identify and sell existing properties where appreciation has already occurred. [paras. 112-13]

The Board went on to conclude that the sharing of the net gain on the sale of the land and buildings collectively, in accordance with the *TransAlta Formula*, was equitable in the circumstances of this application and was consistent with past Board decisions.

The Board determined that from the gross proceeds of $6,550,000, ATCO should receive $465,000 to cover the cost of disposition ($265,000) and the provision for environmental remediation ($200,000), the shareholders should receive $2,014,690, and $4,070,310 should go to the customers. Of the amount credited to shareholders, $225,245 was to be used to remove the remaining net book value of the property from ATCO's accounts. Of the amount allocated to customers, $3,045,813 was allocated to ATCO Gas - South customers and $1,024,497 to ATCO Pipelines - South customers.

1.2.2 Court of Appeal of Alberta ((2004), 24 Alta. L.R. (4th) 205, 2004 ABCA 3)

ATCO appealed the Board's decision. It argued that the Board did not have any jurisdiction to allocate the proceeds of sale and that the proceeds should have been allocated entirely to the shareholders. In its view, allowing customers to share in the proceeds of sale would result in them benefiting twice, since they had been spared the costs of renovating the sold assets and would enjoy cost savings from the lease arrangements. The Court of Appeal of Alberta agreed with ATCO, allowing the appeal and setting aside the Board's decision. The

[TRADUCTION] Il serait avantageux pour les clients de leur attribuer la totalité du profit net tiré de la vente du terrain et des bâtiments, mais cela pourrait dissuader la société de soumettre son fonctionnement à une analyse continue afin de trouver des moyens d'améliorer son rendement et de réduire ses coûts de manière constante.

À l'inverse, attribuer à l'entreprise réglementée la totalité du profit net pourrait encourager la spéculation à l'égard de biens non amortissables ou l'identification des biens dont la valeur s'est déjà accrue et leur aliénation. [par. 112-113]

16 La Commission a poursuivi en concluant que le partage du gain net résultant globalement de la vente du terrain et des bâtiments, selon la *formule TransAlta*, était équitable dans les circonstances et conforme à ses décisions antérieures.

17 Elle a décidé de répartir le produit brut de la vente (6 550 000 $) comme suit : 465 000 $ à ATCO pour les frais d'aliénation (265 000 $) et la dépollution (200 000 $), 2 014 690 $ aux actionnaires et 4 070 310 $ aux clients. Un montant de 225 245 $ devait être prélevé de la somme attribuée aux actionnaires pour radier des registres d'ATCO la valeur comptable nette des biens vendus. De la somme attribuée aux clients, 3 045 813 $ étaient alloués aux clients d'ATCO Gas - South et 1 024 497 $ à ceux d'ATCO Pipelines - South.

1.2.2 La Cour d'appel de l'Alberta ((2004), 24 Alta. L.R. (4th) 205, 2004 ABCA 3)

18 ATCO a interjeté appel de la décision. Elle a fait valoir que la Commission n'avait pas compétence pour attribuer le produit de la vente, qui aurait dû revenir en entier aux actionnaires. Selon elle, en touchant une partie du produit de la vente, les clients gagnaient sur tous les tableaux puisqu'ils n'avaient pas supporté le coût de la rénovation des biens vendus et qu'ils profiteraient d'économies grâce à l'entente de location. La Cour d'appel de l'Alberta lui a donné raison, accueillant l'appel et annulant la décision. Elle a renvoyé l'affaire à la

matter was referred back to the Board, and the Board was directed to allocate the entire amount appearing in Line 11 of the allocation of proceeds, entitled "Remainder to be Shared" to ATCO. For the reasons that follow, the Court of Appeal's decision should be upheld, in part; it did not err when it held that the Board did not have the jurisdiction to allocate the proceeds of the sale to ratepayers.

2. Analysis

2.1 *Issues*

19 There is an appeal and a cross-appeal in this case: an appeal by the City in which it submits that, contrary to the Court of Appeal's decision, the Board had jurisdiction to allocate a portion of the net gain on the sale of a utility asset to the rate-paying customers, even where no harm to the public was found at the time the Board approved the sale, and a cross-appeal by ATCO in which it questions the Board's jurisdiction to allocate any of ATCO's proceeds from the sale to customers. In particular, ATCO contends that the Board has no jurisdiction to make an allocation to rate-paying customers, equivalent to the accumulated depreciation calculated for prior years. No matter how the issue is framed, it is evident that the crux of this appeal lies in whether the Board has the jurisdiction to distribute the gain on the sale of a utility company's asset.

20 Given my conclusion on this issue, it is not necessary for me to consider whether the Board's allocation of the proceeds in this case was reasonable. Nevertheless, as I note at para. 82, I will direct my attention briefly to the question of the exercise of discretion in view of my colleague's reasons.

2.2 *Standard of Review*

21 As this appeal stems from an administrative body's decision, it is necessary to determine the appropriate level of deference which must be shown to the body. Wittmann J.A., writing for the Court of Appeal, concluded that the issue of jurisdiction of the Board attracted a standard of correctness. ATCO concurs with this conclusion. I agree. No deference should be shown for the Board's

Commission, lui enjoignant d'attribuer à ATCO la totalité du solde à répartir selon la ligne 11 du tableau d'attribution du produit de la vente. Pour les motifs qui suivent, il y a lieu de confirmer en partie le jugement de la Cour d'appel, qui n'a pas eu tort de statuer que la Commission n'avait pas le pouvoir d'attribuer le produit de la vente aux clients.

2. Analyse

2.1 *Questions en litige*

Nous sommes saisis d'un pourvoi et d'un pourvoi incident. Dans son pourvoi, la Ville affirme que contrairement à ce qu'a estimé la Cour d'appel, la Commission avait le pouvoir d'attribuer aux clients une partie du gain net résultant de la vente d'un bien affecté au service public même si elle avait conclu, au moment d'autoriser la vente, qu'aucun préjudice ne serait causé au public. Dans son pourvoi incident, ATCO conteste le pouvoir de la Commission d'attribuer aux clients toute partie du produit de la vente. Elle soutient en particulier que la Commission n'a pas le pouvoir de leur attribuer l'équivalent de l'amortissement calculé les années antérieures. Peu importe la formulation de la question en litige, notre Cour est appelée en l'espèce à décider si la Commission a le pouvoir d'attribuer le gain net tiré de la vente d'un bien d'une entreprise de services publics.

Vu la conclusion à laquelle j'arrive, point n'est besoin de se demander si la Commission a raisonnablement réparti le produit de la vente. Néanmoins, comme je le signale au par. 82, vu les motifs de mon collègue, je me penche brièvement sur la question de l'exercice du pouvoir discrétionnaire.

2.2 *Norme de contrôle*

Une décision administrative étant à l'origine du présent pourvoi, il faut déterminer le degré de déférence auquel a droit l'organisme qui l'a rendue. S'exprimant au nom de la Cour d'appel, le juge Wittmann a conclu que la question de la compétence de la Commission commandait l'application de la norme de la décision correcte. ATCO en convient, et moi aussi. Il n'y a pas lieu de faire preuve de

decision with regard to its jurisdiction on the allocation of the net gain on sale of assets. An inquiry into the factors enunciated by this Court in *Pushpanathan v. Canada (Minister of Citizenship and Immigration)*, [1998] 1 S.C.R. 982, confirms this conclusion, as does the reasoning in *United Taxi Drivers' Fellowship of Southern Alberta v. Calgary (City)*, [2004] 1 S.C.R. 485, 2004 SCC 19.

Although it is not necessary to conduct a full analysis of the standard of review in this case, I will address the issue briefly in light of the fact that Binnie J. deals with the exercise of discretion in his reasons for judgment. The four factors that need to be canvassed in order to determine the appropriate standard of review of an administrative tribunal decision are: (1) the existence of a privative clause; (2) the expertise of the tribunal/board; (3) the purpose of the governing legislation and the particular provisions; and (4) the nature of the problem (*Pushpanathan*, at paras. 29-38).

In the case at bar, one should avoid a hasty characterizing of the issue as "jurisdictional" and subsequently be tempted to skip the pragmatic and functional analysis. A complete examination of the factors is required.

First, s. 26(1) of the AEUBA grants a right of appeal, but in a limited way. Appeals are allowed on a question of jurisdiction or law and only after leave to appeal is obtained from a judge:

26(1) Subject to subsection (2), an appeal lies from the Board to the Court of Appeal on a question of jurisdiction or on a question of law.

(2) Leave to appeal may be obtained from a judge of the Court of Appeal only on an application made

(a) within 30 days from the day that the order, decision or direction sought to be appealed from was made, or

(b) within a further period of time as granted by the judge where the judge is of the opinion that the circumstances warrant the granting of that further period of time.

déférence à l'égard de la décision de la Commission concernant son pouvoir d'attribuer le gain net tiré de la vente des biens. L'examen des facteurs énoncés par notre Cour dans l'arrêt *Pushpanathan c. Canada (Ministre de la Citoyenneté et de l'Immigration)*, [1998] 1 R.C.S. 982, confirme cette conclusion, tout comme son raisonnement dans l'arrêt *United Taxi Drivers' Fellowship of Southern Alberta c. Calgary (Ville)*, [2004] 1 R.C.S. 485, 2004 CSC 19.

22 Bien qu'il ne soit pas nécessaire d'approfondir la question de la norme de contrôle applicable en l'espèce, je l'examinerai brièvement puisque, dans ses motifs, le juge Binnie se prononce sur l'exercice du pouvoir discrétionnaire. Les quatre facteurs à considérer pour déterminer la norme de contrôle applicable à la décision d'un tribunal administratif sont les suivants : (1) l'existence d'une clause privative; (2) l'expertise du tribunal ou de l'organisme; (3) l'objet de la loi applicable et des dispositions en cause; (4) la nature du problème (*Pushpanathan*, par. 29-38).

23 Dans la présente affaire, il faut se garder de conclure hâtivement que la question en litige en est une de « compétence » puis de laisser tomber l'analyse pragmatique et fonctionnelle. L'examen exhaustif des facteurs s'impose.

24 Premièrement, le par. 26(1) de l'AEUBA prévoit un droit d'appel restreint qui ne peut être exercé que sur une question de compétence ou de droit et seulement avec l'autorisation d'un juge :

[TRADUCTION]

26(1) Sous réserve du paragraphe (2), les décisions de la Commission sont susceptibles d'appel devant la Cour d'appel sur une question de droit ou de compétence.

(2) L'autorisation d'appel ne peut être obtenue d'un juge de la Cour d'appel que sur demande présentée

a) dans les 30 jours qui suivent l'ordonnance, la décision ou la directive en cause ou

b) dans le délai supplémentaire que le juge estime justifié d'accorder dans les circonstances.

In addition, the AEUBA includes a privative clause which states that every action, order, ruling or decision of the Board is final and shall not be questioned, reviewed or restrained by any proceeding in the nature of an application for judicial review or otherwise in any court (s. 27).

25 The presence of a statutory right of appeal on questions of jurisdiction and law suggests a more searching standard of review and less deference to the Board on those questions (see *Pushpanathan*, at para. 30). However, the presence of the privative clause and right to appeal are not decisive, and one must proceed with the examination of the nature of the question to be determined and the relative expertise of the tribunal in those particular matters.

26 Second, as observed by the Court of Appeal, no one disputes the fact that the Board is a specialized body with a high level of expertise regarding Alberta's energy resources and utilities (see, e.g., *Consumers' Gas Co. v. Ontario (Energy Board)*, [2001] O.J. No. 5024 (QL) (Div. Ct.), at para. 2; *Coalition of Citizens Impacted by the Caroline Shell Plant v. Alberta (Energy Utilities Board)* (1996), 41 Alta. L.R. (3d) 374 (C.A.), at para. 14. In fact, the Board is a permanent tribunal with a long-term regulatory relationship with the regulated utilities.

27 Nevertheless, the Court is concerned not with the general expertise of the administrative decision maker, but with its expertise in relation to the specific nature of the issue before it. Consequently, while normally one would have assumed that the Board's expertise is far greater than that of a court, the nature of the problem at bar, to adopt the language of the Court of Appeal (para. 35), "neutralizes" this deference. As I will elaborate below, the expertise of the Board is not engaged when deciding the scope of its powers.

De plus, l'AEUBA renferme une clause d'immunité de contrôle (ou clause privative) prévoyant que toute mesure, ordonnance ou décision de la Commission est définitive et ne peut être contestée, révisée ou restreinte dans le cadre d'une instance judiciaire, y compris une demande de contrôle judiciaire (art. 27).

Le fait que la loi prévoit un droit d'appel sur une question de compétence ou de droit seulement permet de conclure à l'application d'une norme de contrôle plus stricte et donne à penser que notre Cour doit se montrer moins déférente vis-à-vis de la Commission relativement à ces questions (voir *Pushpanathan*, par. 30). Cependant, l'existence d'une clause d'immunité de contrôle et d'un droit d'appel n'est pas décisive, de sorte qu'il nous faut examiner la nature de la question à trancher et l'expertise relative du tribunal administratif à cet égard.

Deuxièmement, comme l'a fait remarquer la Cour d'appel, nul ne conteste que la Commission est un organisme spécialisé doté d'une grande expertise en ce qui concerne les ressources et les services publics de l'Alberta dans le domaine énergétique (voir, p. ex., *Consumers' Gas Co. c. Ontario (Energy Board)*, [2001] O.J. No. 5024 (QL) (C. div.), par. 2; *Coalition of Citizens Impacted by the Caroline Shell Plant c. Alberta (Energy Utilities Board)* (1996), 41 Alta. L.R. (3d) 374 (C.A.), par. 14. Il s'agit en fait d'un tribunal administratif permanent qui régit depuis nombre d'années les services publics réglementés.

Quoi qu'il en soit, notre Cour s'intéresse non pas à l'expertise générale de l'instance administrative, mais à son expertise quant à la question précise dont elle est saisie. Par conséquent, même si l'on tiendrait normalement pour acquis que l'expertise de la Commission est beaucoup plus grande que celle d'une cour de justice, la nature de la question en litige « neutralise », pour reprendre le terme employé par la Cour d'appel (par. 35), la déférence qu'appelle cette considération. Comme je l'explique plus loin, l'expertise de la Commission n'est pas mise à contribution lorsqu'elle se prononce sur l'étendue de ses pouvoirs.

Third, the present case is governed by three pieces of legislation: the PUBA, the GUA and the AEUBA. These statutes give the Board a mandate to safeguard the public interest in the nature and quality of the service provided to the community by public utilities: *Atco Ltd. v. Calgary Power Ltd.*, [1982] 2 S.C.R. 557, at p. 576; *Dome Petroleum Ltd. v. Public Utilities Board (Alberta)* (1976), 2 A.R. 453 (C.A.), at paras. 20-22, aff'd [1977] 2 S.C.R. 822. The legislative framework at hand has as its main purpose the proper regulation of a gas utility in the public interest, more specifically the regulation of a monopoly in the public interest with its primary tool being rate setting, as I will explain later.

The particular provision at issue, s. 26(2)(d)(i) of the GUA, which requires a utility to obtain the approval of the regulator before it sells an asset, serves to protect the customers from adverse results brought about by any of the utility's transactions by ensuring that the economic benefits to customers are enhanced (MacAvoy and Sidak, at pp. 234-36).

While at first blush the purposes of the relevant statutes and of the Board can be conceived as a delicate balancing between different constituencies, i.e., the utility and the customer, and therefore entail determinations which are polycentric (*Pushpanathan*, at para. 36), the interpretation of the enabling statutes and the particular provisions under review (s. 26(2)(d) of the GUA and s. 15(3)(d) of the AEUBA) is not a polycentric question, contrary to the conclusion of the Court of Appeal. It is an inquiry into whether a proper construction of the enabling statutes gives the Board jurisdiction to allocate the profits realized from the sale of an asset. The Board was not created with the main purpose of interpreting the AEUBA, the GUA or the PUBA in the abstract, where no policy consideration is at issue, but rather to ensure that utility rates are always just and reasonable (see *Atco Ltd.*, at p. 576). In the case at bar, this protective role does not come into play. Hence, this factor points to a less deferential standard of review.

28 Troisièmement, trois lois s'appliquent en l'espèce : la PUBA, la GUA et l'AEUBA. Suivant ces lois, la Commission a pour mission de protéger l'intérêt public quant à la nature et à la qualité des services fournis à la collectivité par les entreprises de services publics : *Atco Ltd. c. Calgary Power Ltd.*, [1982] 2 R.C.S. 557, p. 576; *Dome Petroleum Ltd. c. Public Utilities Board (Alberta)* (1976), 2 A.R. 453 (C.A.), par. 20-22, conf. par [1977] 2 R.C.S. 822. L'objet premier de ce cadre législatif est de réglementer adéquatement un service de gaz dans l'intérêt public ou, plus précisément, de réglementer un monopole dans l'intérêt public, grâce principalement à l'établissement des tarifs. J'y reviendrai.

29 La disposition qui nous intéresse au premier chef, le sous-al. 26(2)d)(i) de la GUA, qui exige qu'un service public obtienne de l'organisme de réglementation l'autorisation de vendre un bien, vise à protéger les clients contre les effets préjudiciables de toute opération de l'entreprise en veillant à l'accroissement des avantages financiers qu'ils en tirent (MacAvoy et Sidak, p. 234-236).

30 Même si, à première vue, on peut considérer que l'objet des lois pertinentes et la raison d'être de la Commission sont de réaliser un équilibre délicat entre divers intéressés — le service public et les clients — et, par conséquent, qu'ils impliquent un processus décisionnel polycentrique (*Pushpanathan*, par. 36), l'interprétation des lois habilitantes et des dispositions en cause (al. 26(2)d) de la GUA et 15(3)d) de l'AEUBA) n'est pas, contrairement à ce qu'a conclu la Cour d'appel, une question polycentrique. Il s'agit plutôt de déterminer si, interprétées correctement, les lois habilitantes confèrent à la Commission le pouvoir d'attribuer le profit tiré de la vente d'un bien. Lorsque aucune question de principe n'est soulevée, le mandat premier de la Commission n'est pas d'interpréter l'AEUBA, la GUA ou la PUBA de manière abstraite, mais de veiller à ce que la tarification soit toujours juste et raisonnable (voir *Atco Ltd.*, p. 576). En l'espèce, ce rôle de protection n'entre pas en jeu. Partant, le troisième facteur commande l'application d'une norme de contrôle moins déférente.

31 Fourth, the nature of the problem underlying each issue is different. The parties are in essence asking the Court to answer two questions (as I have set out above), the first of which is to determine whether the power to dispose of the proceeds of sale falls within the Board's statutory mandate. The Board, in its decision, determined that it had the power to allocate a portion of the proceeds of a sale of utility assets to the ratepayers; it based its decision on its statutory powers, the equitable principles rooted in the "regulatory compact" (see para. 63 of these reasons) and previous practice. This question is undoubtedly one of law and jurisdiction. The Board would arguably have no greater expertise with regard to this issue than the courts. A court is called upon to interpret provisions that have no technical aspect, in contrast with the provision disputed in *Barrie Public Utilities v. Canadian Cable Television Assn.*, [2003] 1 S.C.R. 476, 2003 SCC 28, at para. 86. The interpretation of general concepts such as "public interest" and "conditions" (as found in s. 15(3)(d) of the AEUBA) is not foreign to courts and is not derived from an area where the tribunal has been held to have greater expertise than the courts. The second question is whether the method and actual allocation in this case were reasonable. To resolve this issue, one must consider case law, policy justifications and the practice of other boards, as well as the details of the particular allocation in this case. The issue here is most likely characterized as one of mixed fact and law.

Quatrièmement, la nature du problème n'est pas la même pour chacune des questions en litige. Les parties demandent en substance à notre Cour de répondre à deux questions (énoncées précédemment). Premièrement, le pouvoir d'attribuer le produit de la vente relève-t-il du mandat légal de la Commission? Dans sa décision, cette dernière a statué qu'elle avait le pouvoir d'attribuer aux clients une partie du produit de la vente des biens d'un service public. Elle a invoqué à l'appui ses pouvoirs légaux, les principes d'équité inhérents au « pacte réglementaire » (voir par. 63 des présents motifs) et ses décisions antérieures. Il s'agit clairement d'une question de droit et de compétence. L'on pourrait soutenir que la Commission ne possède pas une plus grande expertise qu'une cour de justice à cet égard. Une cour de justice est appelée à interpréter des dispositions ne comportant aucun aspect technique, ce qui n'était pas le cas de la disposition en litige dans l'arrêt *Barrie Public Utilities c. Assoc. canadienne de télévision par câble*, [2003] 1 R.C.S. 476, 2003 CSC 28, par. 86. Qui plus est, l'interprétation de notions générales comme l'« intérêt public » et l'« imposition de conditions » (que l'on retrouve à l'al. 15(3)d) de l'AEUBA), n'est pas étrangère à une cour de justice et n'appartient pas à un domaine dans lequel il a été jugé qu'un tribunal administratif avait une plus grande expertise qu'une cour de justice. Deuxièmement, la méthode employée en l'espèce et l'attribution en résultant étaient-elles raisonnables? Pour répondre à cette question, il faut examiner la jurisprudence, les considérations de principe et la pratique d'autres organismes, ainsi que le détail de l'attribution en l'espèce. Il s'agit en somme d'une question mixte de fait et de droit.

32 In light of the four factors, I conclude that each question requires a distinct standard of review. To determine the Board's power to allocate proceeds from a sale of utility assets suggests a standard of review of correctness. As expressed by the Court of Appeal, the focus of this inquiry remains on the particular provisions being invoked and interpreted by the tribunal (s. 26(2)(d) of the GUA and s. 15(3)(d) of the AEUBA) and "goes to jurisdiction"

Au vu des quatre facteurs, je conclus que chacune des questions en litige appelle une norme de contrôle distincte. Statuer sur le pouvoir de la Commission d'attribuer le produit de la vente d'un bien d'un service public requiert l'application de la norme de la décision correcte. Comme l'a dit la Cour d'appel, l'accent est mis sur les dispositions invoquées et interprétées par la Commission (al. 26(2)d) de la GUA et 15(3)d) de l'AEUBA) et la

(*Pushpanathan*, at para. 28). Moreover, keeping in mind all the factors discussed, the generality of the proposition will be an additional factor in favour of the imposition of a correctness standard, as I stated in *Pushpanathan*, at para. 38:

> . . . the broader the propositions asserted, and the further the implications of such decisions stray from the core expertise of the tribunal, the less likelihood that deference will be shown. Without an implied or express legislative intent to the contrary as manifested in the criteria above, legislatures should be assumed to have left highly generalized propositions of law to courts.

The second question regarding the Board's actual method used for the allocation of proceeds likely attracts a more deferential standard. On the one hand, the Board's expertise, particularly in this area, its broad mandate, the technical nature of the question and the general purposes of the legislation, all suggest a relatively high level of deference to the Board's decision. On the other hand, the absence of a privative clause on questions of jurisdiction and the reference to law needed to answer this question all suggest a less deferential standard of review which favours reasonableness. It is not necessary, however, for me to determine which specific standard would have applied here.

As will be shown in the analysis below, I am of the view that the Court of Appeal made no error of fact or law when it concluded that the Board acted beyond its jurisdiction by misapprehending its statutory and common law authority. However, the Court of Appeal erred when it did not go on to conclude that the Board has no jurisdiction to allocate *any* portion of the proceeds of sale of the property to ratepayers.

2.3 *Was the Board's Decision as to Its Jurisdiction Correct?*

Administrative tribunals or agencies are statutory creations: they cannot exceed the powers that were granted to them by their enabling statute; they

question « touche la compétence » (*Pushpanathan*, par. 28). De plus, gardant présents à l'esprit tous les facteurs considérés, le caractère général de la proposition est un autre élément qui milite en faveur de la norme de la décision correcte, comme je l'ai dit dans l'arrêt *Pushpanathan* (par. 38) :

> . . . plus les propositions avancées sont générales, et plus les répercussions de ces décisions s'écartent du domaine d'expertise fondamental du tribunal, moins il est vraisemblable qu'on fasse preuve de retenue. En l'absence d'une intention législative implicite ou expresse à l'effet contraire manifestée dans les critères qui précèdent, on présumera que le législateur a voulu laisser aux cours de justice la compétence de formuler des énoncés de droit fortement généralisés.

33 La deuxième question, qui porte sur la méthode employée par la Commission pour attribuer le produit de la vente, appelle vraisemblablement une norme de contrôle plus déférente. D'une part, l'expertise de la Commission, dans ce domaine en particulier, son vaste mandat, la technicité de la question et l'objet général des lois en cause portent à croire que sa décision justifie un degré relativement élevé de déférence. D'autre part, l'absence d'une clause d'immunité de contrôle visant les questions de compétence et la nécessité de se référer au droit pour trancher la question, appellent l'application d'une norme de contrôle moins déférente privilégiant le caractère raisonnable de la décision. Il n'est toutefois pas nécessaire que je précise quelle norme de contrôle aurait été applicable en l'espèce.

34 Comme le montre l'analyse qui suit, je suis d'avis que la Cour d'appel n'a pas commis d'erreur de fait ou de droit lorsqu'elle a conclu que la Commission avait outrepassé sa compétence en se méprenant sur les pouvoirs que lui confèrent la loi et la common law. Cependant, elle a eu tort de ne pas conclure en outre que la Commission n'avait pas le pouvoir d'attribuer aux clients *quelque* partie du produit de la vente des biens.

2.3 *La Commission a-t-elle rendu une décision correcte au sujet de sa compétence?*

35 Un tribunal ou un organisme administratif est une création de la loi : il ne peut outrepasser les pouvoirs que lui confère sa loi habilitante, il doit

must "adhere to the confines of their statutory authority or 'jurisdiction'[; and t]hey cannot trespass in areas where the legislature has not assigned them authority": Mullan, at pp. 9-10 (see also S. Blake, *Administrative Law in Canada* (3rd ed. 2001), at pp. 183-84).

36 In order to determine whether the Board's decision that it had the jurisdiction to allocate proceeds from the sale of a utility's asset was correct, I am required to interpret the legislative framework by which the Board derives its powers and actions.

2.3.1 General Principles of Statutory Interpretation

37 For a number of years now, the Court has adopted E. A. Driedger's modern approach as the method to follow for statutory interpretation (*Construction of Statutes* (2nd ed. 1983), at p. 87):

> Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

(See, e.g., *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27, at para. 21; *Bell ExpressVu Limited Partnership v. Rex*, [2002] 2 S.C.R. 559, 2002 SCC 42, at para. 26; *H.L. v. Canada (Attorney General)*, [2005] 1 S.C.R. 401, 2005 SCC 25, at paras. 186-87; *Marche v. Halifax Insurance Co.*, [2005] 1 S.C.R. 47, 2005 SCC 6, at para. 54; *Barrie Public Utilities*, at paras. 20 and 86; *Contino v. Leonelli-Contino*, [2005] 3 S.C.R. 217, 2005 SCC 63, at para. 19.)

38 But more specifically in the area of administrative law, tribunals and boards obtain their jurisdiction over matters from two sources: (1) express grants of jurisdiction under various statutes (explicit powers); and (2) the common law, by application of the doctrine of jurisdiction by necessary implication (implicit powers) (see also D. M. Brown, *Energy Regulation in Ontario* (loose-leaf ed.), at p. 2-15).

39 The City submits that it is both implicit and explicit within the express jurisdiction that has been

[TRADUCTION] « s'en tenir à son domaine de compétence et ne peut s'immiscer dans un autre pour lequel le législateur ne lui a pas attribué compétence » : Mullan, p. 9-10 (voir également S. Blake, *Administrative Law in Canada* (3e éd. 2001), p. 183-184).

Pour décider si la Commission a eu raison de conclure qu'elle avait le pouvoir d'attribuer le produit de la vente des biens d'un service public, je dois interpréter le cadre législatif à l'origine de ses attributions et de ses actes.

2.3.1 Principes généraux d'interprétation législative

Depuis un certain nombre d'années, notre Cour fait sienne l'approche moderne d'E. A. Driedger en matière d'interprétation des lois (*Construction of Statutes* (2e éd. 1983), p. 87) :

> [TRADUCTION] Aujourd'hui il n'y a qu'un seul principe ou solution : il faut lire les termes d'une loi dans leur contexte global en suivant le sens ordinaire et grammatical qui s'harmonise avec l'esprit de la loi, l'objet de la loi et l'intention du législateur.

(Voir, p. ex., *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 R.C.S. 27, par. 21; *Bell ExpressVu Limited Partnership c. Rex*, [2002] 2 R.C.S. 559, 2002 CSC 42, par. 26; *H.L. c. Canada (Procureur général)*, [2005] 1 R.C.S. 401, 2005 CSC 25, par. 186-187; *Marche c. Cie d'Assurance Halifax*, [2005] 1 R.C.S. 47, 2005 CSC 6, par. 54; *Barrie Public Utilities*, par. 20 et 86; *Contino c. Leonelli-Contino*, [2005] 3 R.C.S. 217, 2005 CSC 63, par. 19.)

Toutefois, dans le domaine du droit administratif, plus particulièrement, la compétence des tribunaux et des organismes administratifs a deux sources : (1) l'octroi exprès par une loi (pouvoir explicite) et (2) la common law, suivant la doctrine de la déduction nécessaire (pouvoir implicite) (voir également D. M. Brown, *Energy Regulation in Ontario* (éd. feuilles mobiles), p. 2-15).

La Ville soutient que le pouvoir exprès de la Commission d'autoriser la vente des biens d'un

conferred upon the Board to approve or refuse to approve the sale of utility assets, that the Board can determine how to allocate the proceeds of the sale in this case. ATCO retorts that not only is such a power absent from the explicit language of the legislation, but it cannot be "implied" from the statutory regime as necessarily incidental to the explicit powers. I agree with ATCO's submissions and will elaborate in this regard.

2.3.2 Explicit Powers: Grammatical and Ordinary Meaning

As a preliminary submission, the City argues that given that ATCO applied to the Board for approval of both the sale transaction *and* the disposition of the proceeds of sale, this suggests that ATCO recognized that the Board has authority to allocate the proceeds as a condition of a proposed sale. This argument does not hold any weight in my view. First, the application for approval cannot be considered on its own an admission by ATCO of the jurisdiction of the Board. In any event, an admission of this nature would not have any bearing on the applicable law. Moreover, knowing that in the past the Board had decided that it had jurisdiction to allocate the proceeds of a sale of assets and had acted on this power, one can assume that ATCO was asking for the approval of the disposition of the proceeds should the Board not accept their argument on jurisdiction. In fact, a review of past Board decisions on the approval of sales shows that utility companies have constantly challenged the Board's jurisdiction to allocate the net gain on the sale of assets (see, e.g., *Re TransAlta Utilities Corp.*, Alta. E.U.B., Decision 2000-41; *Re ATCO Gas-North*, Alta. E.U.B., Decision 2001-65; *Re Alberta Government Telephones*, Alta. P.U.B., Decision No. E84081, June 29, 1984; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84116, October 12, 1984; *TransAlta Utilities Corp. (Re)*, [2002] A.E.U.B.D. No. 30 (QL); *ATCO Electric Ltd. (Re)*, [2003] A.E.U.B.D. No. 92 (QL)).

The starting point of the analysis requires that the Court examine the ordinary meaning of the sections at the centre of the dispute, s. 26(2)(d)(i) of the GUA, ss. 15(1) and 15(3)(d) of the AEUBA and

service public englobe — implicitement et explicitement — celui de décider de l'attribution du produit de la vente. ATCO réplique que non seulement ce pouvoir n'est pas expressément prévu par la loi, mais qu'on ne peut « déduire » du régime législatif qu'il découle nécessairement du pouvoir exprès. Je suis d'accord avec elle et voici pourquoi.

2.3.2 Pouvoir explicite : sens grammatical et ordinaire

40 La Ville soutient à titre préliminaire qu'en lui demandant d'autoriser la vente des biens *et* l'attribution du produit de l'opération, ATCO a reconnu le pouvoir de la Commission d'imposer, comme condition de l'autorisation, une certaine attribution du produit de la vente projetée. À mon avis, l'argument ne tient pas. D'abord, la demande d'autorisation ne peut à elle seule être considérée comme une reconnaissance de la compétence de la Commission. De toute manière, une telle reconnaissance ne serait pas déterminante quant au droit applicable. De plus, sachant que, par le passé, la Commission avait jugé être investie du pouvoir d'attribuer le produit de la vente et avait exercé ce pouvoir, on peut présumer qu'ATCO lui a demandé d'autoriser l'attribution du produit de la vente pour le cas où elle rejetterait sa prétention relative à la compétence. En fait, il appert des décisions antérieures de la Commission d'autoriser ou non une opération que les entreprises de services publics contestent systématiquement son pouvoir d'attribuer le gain net en résultant (voir, p. ex., *Re TransAlta Utilities Corp.*, Alta. E.U.B., Décision 2000-41; *Re ATCO Gas-North*, Alta. E.U.B., Décision 2001-65; *Re Alberta Government Telephones*, Alta. P.U.B., Décision n^{o} E84081, 29 juin 1984; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision n^{o} E84116, 12 octobre 1984; *TransAlta Utilities Corp. (Re)*, [2002] A.E.U.B.D. No. 30 (QL); *ATCO Electric Ltd. (Re)*, [2003] A.E.U.B.D. No. 92 (QL)).

41 L'analyse exige au départ qu'on se penche sur le sens ordinaire des dispositions au cœur du litige, savoir le sous-al. 26(2)d)(i) de la GUA, le par. 15(1) et l'al. 15(3)d) de l'AEUBA et l'art. 37 de la

s. 37 of the PUBA. For ease of reference, I reproduce these provisions:

GUA

26. . . .

(2) No owner of a gas utility designated under subsection (1) shall

. . .

(d) without the approval of the Board,

(i) sell, lease, mortgage or otherwise dispose of or encumber its property, franchises, privileges or rights, or any part of it or them

. . .

and a sale, lease, mortgage, disposition, encumbrance, merger or consolidation made in contravention of this clause is void, but nothing in this clause shall be construed to prevent in any way the sale, lease, mortgage, disposition, encumbrance, merger or consolidation of any of the property of an owner of a gas utility designated under subsection (1) in the ordinary course of the owner's business.

AEUBA

15(1) For the purposes of carrying out its functions, the Board has all the powers, rights and privileges of the ERCB [Energy Resources Conservation Board] and the PUB [Public Utilities Board] that are granted or provided for by any enactment or by law.

. . .

(3) Without restricting subsection (1), the Board may do all or any of the following:

. . .

(d) with respect to an order made by the Board, the ERCB or the PUB in respect of matters referred to in clauses (a) to (c), make any further order and impose any additional conditions that the Board considers necessary in the public interest;

. . .

PUBA. Pour faciliter leur consultation, en voici le texte :

[TRADUCTION]

GUA

26. . . .

(2) Le propriétaire d'un service de gaz désigné en application du paragraphe (1) ne peut

. . .

d) sans l'autorisation de la Commission,

(i) aliéner ou grever ses biens, concessions, privilèges ou droits, en tout ou en partie, notamment en les vendant, en les louant ou en les hypothéquant,

. . .

tout grèvement, vente, location, constitution d'hypothèque, aliénation, regroupement ou fusion intervenant en contravention de la présente disposition est nul, sauf s'il intervient dans le cours normal des activités de l'entreprise.

AEUBA

15(1) Dans l'exercice de ses fonctions, la Commission jouit des pouvoirs, des droits et des privilèges qu'un texte législatif ou le droit par ailleurs applicable confère à l'ERCB [Energy Resources Conservation Board] et à la PUB [Public Utilities Board].

. . .

(3) Sans limiter la portée du paragraphe (1), la Commission peut prendre les mesures suivantes, en totalité ou en partie :

. . .

d) à l'égard d'une ordonnance rendue par elle, l'ERCB ou la PUB en application des alinéas a) à c), rendre toute autre ordonnance et imposer les conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public;

. . .

PUBA

37 In matters within its jurisdiction the Board may order and require any person or local authority to do forthwith or within or at a specified time and in any manner prescribed by the Board, so far as it is not inconsistent with this Act or any other Act conferring jurisdiction, any act, matter or thing that the person or local authority is or may be required to do under this Act or under any other general or special Act, and may forbid the doing or continuing of any act, matter or thing that is in contravention of any such Act or of any regulation, rule, order or direction of the Board.

Some of the above provisions are duplicated in the other two statutes (see, e.g., PUBA, ss. 85(1) and 101(2)(d)(i); GUA, s. 22(1); see Appendix).

There is no dispute that s. 26(2) of the GUA contains a prohibition against, among other things, the owner of a utility selling, leasing, mortgaging or otherwise disposing of its property outside of the ordinary course of business without the approval of the Board. As submitted by ATCO, the power conferred is to approve without more. There is no mention in s. 26 of the grounds for granting or denying approval or of the ability to grant conditional approval, let alone the power of the Board to allocate the net profit of an asset sale. I would note in passing that this power is sufficient to alleviate the fear expressed by the Board that the utility might be tempted to sell assets on which it might realize a large profit to the detriment of ratepayers if it could reap the benefits of the sale.

It is interesting to note that s. 26(2) does not apply to all types of sales (and leases, mortgages, dispositions, encumbrances, mergers or consolidations). It excludes sales in the ordinary course of the owner's business. If the statutory scheme was such that the Board had the power to allocate the proceeds of the sale of utility assets, as argued here, s. 26(2) would naturally apply to all sales of assets or, at a minimum, exempt only those sales below a certain value. It is apparent that allocation of sale proceeds to customers is not one of its purposes. In fact, s. 26(2) can only have limited, if any, application to non-utility assets not related to utility function (especially when the sale has passed the "no-harm"

PUBA

37 Dans les domaines de sa compétence, la Commission peut ordonner et exiger qu'une personne, y compris une administration municipale, immédiatement ou dans le délai qu'elle impartit et selon les modalités qu'elle détermine, à condition que ce ne soit pas incompatible avec la présente loi ou une autre conférant compétence, fasse ce qu'elle est tenue de faire ou susceptible d'être tenue de faire suivant la présente loi ou toute autre, générale ou spéciale, et elle peut interdire ou faire cesser tout ce qui contrevient à ces lois ou à ses règles, ses ordonnances ou ses directives.

42 Certaines de ces dispositions figurent également dans les deux autres lois (voir, p. ex., le par. 85(1) et le sous-al. 101(2)d)(i) de la PUBA; le par. 22(1) de la GUA; texte en annexe).

43 Nul ne conteste que le par. 26(2) de la GUA interdit entre autres au propriétaire d'un service public d'aliéner ses biens, notamment par vente, location ou constitution d'hypothèque, sans l'autorisation de la Commission, sauf dans le cours normal des activités de l'entreprise. Comme l'a fait valoir ATCO, la Commission a le pouvoir d'autoriser l'opération, sans plus. L'article 26 ne fait aucune mention des raisons pour lesquelles l'autorisation peut être accordée ou refusée ni de la faculté d'autoriser l'opération à certaines conditions, encore moins du pouvoir d'attribuer le profit net réalisé. Je signale au passage que le pouvoir conféré au par. 26(2) suffit à dissiper la crainte de la Commission que le service public soit tenté de vendre ses biens à fort profit, au détriment des clients, si le bénéfice tiré de la vente lui revient entièrement.

44 Il est intéressant de noter que le par. 26(2) ne s'applique pas à tous les types de vente (ainsi que de location, de constitution d'hypothèque, d'aliénation, de grèvement ou de fusion). En effet, il prévoit une exception pour la vente effectuée dans le cours normal des activités de l'entreprise. Si le régime législatif conférait à la Commission le pouvoir d'attribuer le produit de la vente des biens d'un service public, comme on le prétend en l'espèce, il va de soi que le par. 26(2) s'appliquerait à toute vente de biens ou, à tout le moins, ne prévoirait une exception que pour la vente n'excédant pas un certain montant. Il appert que l'attribution du produit de la vente aux clients n'est pas l'un de ses objets.

test). The provision can only be meant to ensure that the asset in question is indeed non-utility, so that its loss does not impair the utility function or quality.

45 Therefore, a simple reading of s. 26(2) of the GUA does permit one to conclude that the Board does not have the power to allocate the proceeds of an asset sale.

46 The City does not limit its arguments to s. 26(2); it also submits that the AEUBA, pursuant to s. 15(3), is an express grant of jurisdiction because it authorizes the Board to impose any condition to any order so long as the condition is necessary in the public interest. In addition, it relies on the general power in s. 37 of the PUBA for the proposition that the Board may, in any matter within its jurisdiction, make any order pertaining to that matter that is not inconsistent with any applicable statute. The intended meaning of these two provisions, however, is lost when the provisions are simply read in isolation as proposed by the City: R. Sullivan, *Sullivan and Driedger on the Construction of Statutes* (4th ed. 2002), at p. 21; *Canadian Pacific Air Lines Ltd. v. Canadian Air Line Pilots Assn.*, [1993] 3 S.C.R. 724, at p. 735; *Marche*, at paras. 59-60; *Bristol-Myers Squibb Co. v. Canada (Attorney General)*, [2005] 1 S.C.R. 533, 2005 SCC 26, at para. 105. These provisions on their own are vague and open-ended. It would be absurd to allow the Board an unfettered discretion to attach any condition it wishes to an order it makes. Furthermore, the concept of "public interest" found in s. 15(3) is very wide and elastic; the Board cannot be given total discretion over its limitations.

47 While I would conclude that the legislation is silent as to the Board's power to deal with sale

D'ailleurs, en ce qui concerne les biens non affectés au service public et étrangers à la prestation du service, l'application de cette disposition, à supposer qu'elle s'applique, est nécessairement limitée (surtout lorsque la vente satisfait au critère de l'« absence de préjudice »). Le paragraphe 26(2) ne peut avoir qu'un seul objet, soit garantir que le bien n'est pas affecté au service public, de manière que son aliénation ne nuise ni à la prestation du service ni à sa qualité.

Par conséquent, la simple lecture du par. 26(2) de la GUA permet de conclure que la Commission n'a pas le pouvoir d'attribuer le produit de la vente d'un bien.

La Ville ne fonde pas son argumentation que sur le par. 26(2); elle fait aussi valoir que le par. 15(3) de l'AEUBA, qui autorise la Commission à assortir ses ordonnances des conditions qu'elle estime nécessaires dans l'intérêt public, confère un pouvoir exprès à la Commission. De plus, elle invoque le pouvoir général que prévoit l'art. 37 de la PUBA pour soutenir que la Commission peut, dans les domaines de sa compétence, rendre toute ordonnance qui n'est pas incompatible avec une disposition législative applicable. Or, considérer ces deux dispositions isolément comme le préconise la Ville fait perdre de vue leur véritable portée : R. Sullivan, *Sullivan and Driedger on the Construction of Statutes* (4e éd. 2002), p. 21; *Lignes aériennes Canadien Pacifique Ltée c. Assoc. canadienne des pilotes de lignes aériennes*, [1993] 3 R.C.S. 724, p. 735; *Marche*, par. 59-60; *Bristol-Myers Squibb Co. c. Canada (Procureur général)*, [2005] 1 R.C.S. 533, 2005 CSC 26, par. 105. En eux-mêmes, le par. 15(3) et l'art. 37 sont vagues et sujets à diverses interprétations. Il serait absurde d'accorder à la Commission le pouvoir discrétionnaire absolu d'assortir ses ordonnances des conditions de son choix. De plus, la notion d'« intérêt public » à laquelle renvoie le par. 15(3) est très large et élastique; la Commission ne peut se voir accorder le pouvoir discrétionnaire absolu d'en circonscrire les limites.

Même si, à l'issue de la première étape du processus d'interprétation législative, je suis enclin à

proceeds after the initial stage in the statutory interpretation analysis, because the provisions can nevertheless be said to reveal some ambiguity and incoherence, I will pursue the inquiry further.

This Court has stated on numerous occasions that the grammatical and ordinary sense of a section is not determinative and does not constitute the end of the inquiry. The Court is obliged to consider the total context of the provisions to be interpreted, no matter how plain the disposition may seem upon initial reading (see *Chieu v. Canada (Minister of Citizenship and Immigration)*, [2002] 1 S.C.R. 84, 2002 SCC 3, at para. 34; Sullivan, at pp. 20-21). I will therefore proceed to examine the purpose and scheme of the legislation, the legislative intent and the relevant legal norms.

2.3.3 Implicit Powers: Entire Context

The provisions at issue are found in statutes which are themselves components of a larger statutory scheme which cannot be ignored:

> As the product of a rational and logical legislature, the statute is considered to form a system. Every component contributes to the meaning as a whole, and the whole gives meaning to its parts: "each legal provision should be considered in relation to other provisions, as parts of a whole" . . . .
>
> (P.-A. Côté, *The Interpretation of Legislation in Canada* (3rd ed. 2000), at p. 308)

As in any statutory interpretation exercise, when determining the powers of an administrative body, courts need to examine the context that colours the words and the legislative scheme. The ultimate goal is to discover the clear intent of the legislature and the true purpose of the statute while preserving the harmony, coherence and consistency of the legislative scheme (*Bell ExpressVu*, at para. 27; see also *Interpretation Act*, R.S.A. 2000, c. I-8, s. 10 (in Appendix)). "[S]tatutory interpretation is the art of finding the legislative spirit embodied in enactments": *Bristol-Myers Squibb Co.*, at para. 102.

conclure que la loi est silencieuse en ce qui concerne le pouvoir de la Commission de décider du sort du produit de la vente, je poursuis l'analyse car on peut néanmoins soutenir que les dispositions sont jusqu'à un certain point ambiguës et incohérentes.

48 Notre Cour a affirmé maintes fois que le sens grammatical et ordinaire d'une disposition n'est pas déterminant et ne met pas fin à l'analyse. Il faut tenir compte du contexte global de la disposition, même si, à première vue, le sens de son libellé peut paraître évident (voir *Chieu c. Canada (Ministre de la Citoyenneté et de l'Immigration)*, [2002] 1 R.C.S. 84, 2002 CSC 3, par. 34; Sullivan, p. 20-21). Je vais donc examiner l'objet et l'esprit des lois habilitantes, l'intention du législateur et les normes juridiques pertinentes.

2.3.3 Pouvoir implicite : contexte global

49 Les dispositions en cause figurent dans des lois qui font elles-mêmes partie d'un cadre législatif plus large dont on ne peut faire abstraction :

> Œuvre d'un législateur rationnel et logique, la loi est censée former un système : chaque élément contribue au sens de l'ensemble et l'ensemble, au sens de chacun des éléments : « chaque disposition légale doit être envisagée, relativement aux autres, comme la fraction d'un ensemble complet » . . .
>
> (P.-A. Côté, *Interprétation des lois* (3e éd. 1999), p. 388)

Comme dans le cadre de toute interprétation législative, appelée à circonscrire les pouvoirs d'un organisme administratif, une cour de justice doit tenir compte du contexte qui colore les mots et du cadre législatif. L'objectif ultime consiste à dégager l'intention manifeste du législateur et l'objet véritable de la loi tout en préservant l'harmonie, la cohérence et l'uniformité des lois en cause (*Bell ExpressVu*, par. 27; voir également l'*Interpretation Act*, R.S.A. 2000, ch. I-8, art. 10, à l'annexe). « L'interprétation législative est [. . .] l'art de découvrir l'esprit du législateur qui imprègne les textes législatifs » : *Bristol-Myers Squibb Co.*, par. 102.

50 Consequently, a grant of authority to exercise a discretion as found in s. 15(3) of the AEUBA and s. 37 of the PUBA does not confer unlimited discretion to the Board. As submitted by ATCO, the Board's discretion is to be exercised within the confines of the statutory regime and principles generally applicable to regulatory matters, for which the legislature is assumed to have had regard in passing that legislation (see Sullivan, at pp. 154-55). In the same vein, it is useful to refer to the following passage from *Bell Canada v. Canada (Canadian Radio-Television and Telecommunications Commission)*, [1989] 1 S.C.R. 1722, at p. 1756:

> The powers of any administrative tribunal must of course be stated in its enabling statute but they may also exist by necessary implication from the wording of the act, its structure and its purpose. Although courts must refrain from unduly broadening the powers of such regulatory authorities through judicial law-making, they must also avoid sterilizing these powers through overly technical interpretations of enabling statutes.

51 The mandate of this Court is to determine and apply the intention of the legislature (*Bell ExpressVu*, at para. 62) without crossing the line between judicial interpretation and legislative drafting (see *R. v. McIntosh*, [1995] 1 S.C.R. 686, at para. 26; *Bristol-Myers Squibb Co.*, at para. 174). That being said, this rule allows for the application of the "doctrine of jurisdiction by necessary implication"; the powers conferred by an enabling statute are construed to include not only those expressly granted but also, by implication, all powers which are practically necessary for the accomplishment of the object intended to be secured by the statutory regime created by the legislature (see Brown, at p. 2-16.2; *Bell Canada*, at p. 1756). Canadian courts have in the past applied the doctrine to ensure that administrative bodies have the necessary jurisdiction to accomplish their statutory mandate:

> When legislation attempts to create a comprehensive regulatory framework, the tribunal must have the powers which by practical necessity and necessary implication flow from the regulatory authority explicitly conferred upon it.

Le pouvoir discrétionnaire que le par. 15(3) de l'AEUBA et l'art. 37 de la PUBA confèrent à la Commission n'est donc pas absolu. Comme le dit ATCO, la Commission doit l'exercer en respectant le cadre législatif et les principes généralement applicables en matière de réglementation, dont le législateur est présumé avoir tenu compte en adoptant ces lois (voir Sullivan, p. 154-155). Dans le même ordre d'idées, le passage suivant de l'arrêt *Bell Canada c. Canada (Conseil de la radiodiffusion et des télécommunications canadiennes)*, [1989] 1 R.C.S. 1722, p. 1756, se révèle pertinent :

> Les pouvoirs d'un tribunal administratif doivent évidemment être énoncés dans sa loi habilitante, mais ils peuvent également découler implicitement du texte de la loi, de son économie et de son objet. Bien que les tribunaux doivent s'abstenir de trop élargir les pouvoirs de ces organismes de réglementation par législation judiciaire, ils doivent également éviter de les rendre stériles en interprétant les lois habilitantes de façon trop formaliste.

Il incombe à notre Cour de déterminer l'intention du législateur et d'y donner effet (*Bell ExpressVu*, par. 62) sans franchir la ligne qui sépare l'interprétation judiciaire de la formulation législative (voir *R. c. McIntosh*, [1995] 1 R.C.S. 686, par. 26; *Bristol-Myers Squibb Co.*, par. 174). Cela dit, cette règle permet l'application de « la doctrine de la compétence par déduction nécessaire » : sont compris dans les pouvoirs conférés par la loi habilitante non seulement ceux qui y sont expressément énoncés, mais aussi, par déduction, tous ceux qui sont de fait nécessaires à la réalisation de l'objectif du régime législatif : voir Brown, p. 2-16.2; *Bell Canada*, p. 1756. Par le passé, les cours de justice canadiennes ont appliqué la doctrine de manière à investir les organismes administratifs de la compétence nécessaire à l'exécution de leur mandat légal :

> [TRADUCTION] Lorsque l'objet de la législation est de créer un vaste cadre réglementaire, le tribunal administratif doit posséder les pouvoirs qui, par nécessité pratique et déduction nécessaire, découlent du pouvoir réglementaire qui lui est expressément conféré.

Re Dow Chemical Canada Inc. and Union Gas Ltd. (1982), 141 D.L.R. (3d) 641 (Ont. H.C.), at pp. 658-59, aff'd (1983), 42 O.R. (2d) 731 (C.A.) (see also *Interprovincial Pipe Line Ltd. v. National Energy Board*, [1978] 1 F.C. 601 (C.A.); *Canadian Broadcasting League v. Canadian Radio-television and Telecommunications Commission*, [1983] 1 F.C. 182 (C.A.), aff'd [1985] 1 S.C.R. 174).

I understand the City's arguments to be as follows: (1) the customers acquire a right to the property of the owner of the utility when they pay for the service and are therefore entitled to a return on the profits made at the time of the sale of the property; and (2) the Board has, by necessity, because of its jurisdiction to approve or refuse to approve the sale of utility assets, the power to allocate the proceeds of the sale as a condition of its order. The doctrine of jurisdiction by necessary implication is at the heart of the City's second argument. I cannot accept either of these arguments which are, in my view, diametrically contrary to the state of the law. This is revealed when we scrutinize the entire context which I will now endeavour to do.

After a brief review of a few historical facts, I will probe into the main function of the Board, rate setting, and I will then explore the incidental powers which can be derived from the context.

2.3.3.1 *Historical Background and Broader Context*

The history of public utilities regulation in Alberta originated with the creation in 1915 of the Board of Public Utility Commissioners by *The Public Utilities Act*, S.A. 1915, c. 6. This statute was based on similar American legislation: H. R. Milner, "Public Utility Rate Control in Alberta" (1930), 8 *Can. Bar Rev.* 101, at p. 101. While the American jurisprudence and texts in this area should be considered with caution given that Canada and the United States have very different political and constitutional-legal regimes, they do shed some light on the issue.

Pursuant to *The Public Utilities Act*, the first public utility board was established as a

Re Dow Chemical Canada Inc. and Union Gas Ltd. (1982), 141 D.L.R. (3d) 641 (H.C. Ont.), p. 658-659, conf. par (1983), 42 O.R. (2d) 731 (C.A.) (voir également *Interprovincial Pipe Line Ltd. c. Office national de l'énergie*, [1978] 1 C.F. 601 (C.A.); *Ligue de la radiodiffusion canadienne c. Conseil de la radiodiffusion et des télécommunications canadiennes*, [1983] 1 C.F. 182 (C.A.), conf. par [1985] 1 R.C.S. 174).

52 Voici quelles sont selon moi les prétentions de la Ville : (1) en acquittant leurs factures, les clients acquièrent un droit sur les biens du propriétaire du service public et ont donc droit à une partie du profit tiré de leur vente; (2) le pouvoir de la Commission d'autoriser ou non la vente des biens d'un service public emporte, par nécessité, celui d'assujettir l'autorisation à une certaine répartition du produit de la vente. La doctrine de la compétence par déduction nécessaire est au cœur de la deuxième prétention de la Ville. Je ne peux faire droit ni à l'une ni à l'autre de ces prétentions qui, à mon avis, sont diamétralement contraires au droit applicable, comme le révèle ci-après l'examen du contexte global.

53 Après un bref rappel historique, je me pencherai sur la principale fonction de la Commission, l'établissement des tarifs, puis sur les pouvoirs accessoires qui peuvent être déduits du contexte.

2.3.3.1 *Historique et contexte général*

54 Les services publics sont réglementés en Alberta depuis la création en 1915 de l'organisme appelé Board of Public Utility Commissioners en vertu de la loi intitulée *The Public Utilities Act*, S.A. 1915, ch. 6, inspirée d'une loi américaine similaire : H. R. Milner, « Public Utility Rate Control in Alberta » (1930), 8 *R. du B. can.* 101, p. 101. Bien qu'il faille aborder avec circonspection la jurisprudence et la doctrine américaines dans ce domaine — les régimes politiques des États-Unis et du Canada étant fort différents, tout comme leurs régimes de droit constitutionnel —, elles éclairent la question.

55 Suivant *The Public Utilities Act*, la première commission des services publics, composée de

three-member tribunal to provide general supervision of all public utilities (s. 21), to investigate rates (s. 23), to make orders regarding equipment (s. 24), and to require every public utility to file with it complete schedules of rates (s. 23). Of interest for our purposes, the 1915 statute also required public utilities to obtain the approval of the Board of Public Utility Commissioners before selling any property when outside the ordinary course of their business (s. 29(g)).

56 The Alberta Energy and Utilities Board was created in February 1995 by the amalgamation of the Energy Resources Conservation Board and the Public Utilities Board (see Canadian Institute of Resources Law, *Canada Energy Law Service: Alberta* (loose-leaf ed.), at p. 30-3101). Since then, all matters under the jurisdiction of the Energy Resources Conservation Board and the Public Utilities Board have been handled by the Alberta Energy and Utilities Board and are within its exclusive jurisdiction. The Board has all of the powers, rights and privileges of its two predecessor boards (AEUBA, ss. 13, 15(1); GUA, s. 59).

57 In addition to the powers found in the 1915 statute, which have remained virtually the same in the present PUBA, the Board now benefits from the following express powers to:

1. make an order respecting the improvement of the service or commodity (PUBA, s. 80(b));

2. approve the issue by the public utility of shares, stocks, bonds and other evidences of indebtedness (GUA, s. 26(2)(a); PUBA, s. 101(2)(a));

3. approve the lease, mortgage, disposition or encumbrance of the public utility's property, franchises, privileges or rights (GUA, s. 26(2)(d)(i); PUBA, s. 101(2)(d)(i));

4. approve the merger or consolidation of the public utility's property, franchises, privileges or rights (GUA, s. 26(2)(d)(ii); PUBA, s. 101(2)(d)(ii)); and

trois membres, surveillait de manière générale tous les services publics (art. 21), enquêtait sur les tarifs (art. 23), rendait des ordonnances concernant l'équipement (art. 24) et exigeait que chacun des services publics lui remette la liste complète de ses tarifs (art. 23). Signalons pour les besoins du présent pourvoi que la loi de 1915 exigeait également d'un service public qu'il obtienne de l'organisme l'autorisation de vendre un bien en dehors du cours normal de ses activités (al. 29g)).

La Commission a été créée en février 1995 par le fusionnement de l'Energy Resources Conservation Board et de la Public Utilities Board (voir Institut canadien du droit des ressources, *Canada Energy Law Service : Alberta* (éd. feuilles mobiles), p. 30-3101). Dès lors, toutes les affaires qui étaient du ressort des organismes fusionnés relevaient de sa compétence exclusive. La Commission a tous les pouvoirs, les droits et les privilèges des organismes auxquels elle a succédé (AEUBA, art. 13, par. 15(1); GUA, art. 59).

Outre les pouvoirs prévus dans la loi de 1915, qui sont pratiquement identiques à ceux que confère actuellement la PUBA, la Commission est aujourd'hui investie des pouvoirs exprès suivants :

1. rendre une ordonnance concernant l'amélioration du service ou du produit (PUBA, al. 80b));

2. autoriser l'entreprise de services publics à émettre des actions, des obligations ou d'autres titres d'emprunt (GUA, al. 26(2)a); PUBA, al. 101(2)a));

3. autoriser l'entreprise de services publics à aliéner ou à grever ses biens, concessions, privilèges ou droits, notamment en les louant ou en les hypothéquant (GUA, sous-al. 26(2)d)(i); PUBA, sous-al. 101(2)d)(i));

4. autoriser la fusion ou le regroupement des biens, concessions, privilèges ou droits de l'entreprise de services publics (GUA, sous-al. 26(2)d)(ii); PUBA, sous-al. 101(2)d)(ii));

5. authorize the sale or permit to be made on the public utility's book a transfer of any share of its capital stock to a corporation that would result in the vesting in that corporation of more than 50 percent of the outstanding capital stock of the owner of the public utility (GUA, s. 27(1); PUBA, s. 102(1)).

5. autoriser la vente d'actions de l'entreprise de services publics à une société ou l'inscription dans ses registres de toute cession d'actions à une société lorsque la vente ou la cession ferait en sorte que cette société détienne plus de 50 pour 100 des actions en circulation du propriétaire de l'entreprise de services publics (GUA, par. 27(1); PUBA, par. 102(1)).

It goes without saying that public utilities are very limited in the actions they can take, as evidenced from the above list. Nowhere is there a mention of the authority to allocate proceeds from a sale or the discretion of the Board to interfere with ownership rights.

58 Il appert donc de cette énumération qu'une entreprise de services publics a une marge de manœuvre très limitée. Il n'est fait mention ni du pouvoir d'attribuer le produit de la vente ni du pouvoir discrétionnaire de porter atteinte au droit de propriété.

Even in 1995 when the legislature decided to form the Alberta Energy and Utilities Board, it did not see fit to modify the PUBA or the GUA to provide the new Board with the power to allocate the proceeds of a sale even though the controversy surrounding this issue was full-blown (see, e.g., *Re Alberta Government Telephones*, Alta. P.U.B., Decision No. E84081; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84116). It is a well-established principle that the legislature is presumed to have a mastery of existing law, both common law and statute law (see Sullivan, at pp. 154-55). It is also presumed to have known all of the circumstances surrounding the adoption of new legislation.

59 Même lorsque le législateur a décidé de créer la Commission en 1995, il n'a pas jugé opportun de modifier la PUBA ou la GUA pour donner au nouvel organisme le pouvoir d'attribuer le produit d'une vente. Pourtant, la question suscitait déjà la controverse (voir, p. ex., *Re Alberta Government Telephones*, Alta. P.U.B., Décision n^{o} E84081, et *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision n^{o} E84116). Selon un principe bien établi, le législateur est présumé connaître parfaitement le droit existant, qu'il s'agisse de la common law ou du droit d'origine législative (voir Sullivan, p. 154-155). Il est également censé être au fait de toutes les circonstances entourant l'adoption de la nouvelle loi.

Although the Board may seem to possess a variety of powers and functions, it is manifest from a reading of the AEUBA, the PUBA and the GUA that the principal function of the Board in respect of public utilities is the determination of rates. Its power to supervise the finances of these companies and their operations, although wide, is in practice incidental to fixing rates (see Milner, at p. 102; Brown, at p. 2-16.6). Estey J., speaking for the majority of this Court in *Atco Ltd.*, at p. 576, echoed this view when he said:

60 Bien que la Commission puisse sembler posséder toute une gamme d'attributions et de fonctions, il ressort de l'AEUBA, de la PUBA et de la GUA que son principal mandat, à l'égard des entreprises de services publics, est l'établissement de tarifs. Son pouvoir de surveiller les finances et le fonctionnement de ces entreprises est certes vaste mais, en pratique, il est accessoire à sa fonction première (voir Milner, p. 102; Brown, p. 2-16.6). S'exprimant au nom des juges majoritaires dans *Atco Ltd.*, le juge Estey a abondé dans ce sens (p. 576) :

It is evident from the powers accorded to the Board by the legislature in both statutes mentioned above that the legislature has given the Board a mandate of the widest proportions to safeguard the public interest in the nature and quality of the service provided to the

Il ressort des pouvoirs que le législateur a accordé[s] à la Commission dans les deux lois mentionnées ci-dessus, qu'il a investi la Commission du mandat très général de veiller aux intérêts du public quant à la nature et à la qualité des services rendus à la collectivité par

community by the public utilities. Such an extensive regulatory pattern must, for its effectiveness, include the right to control the combination or, as the legislature says, "the union" of existing systems and facilities. This no doubt has a direct relationship with the rate-fixing function which ranks high in the authority and functions assigned to the Board. [Emphasis added.]

In fact, even the Board itself, on its website (http://www.eub.gov.ab.ca/BBS/eubinfo/default.htm), describes its functions as follows:

> We regulate the safe, responsible, and efficient development of Alberta's energy resources: oil, natural gas, oil sands, coal, and electrical energy; and the pipelines and transmission lines to move the resources to market. On the utilities side, we regulate rates and terms of service of investor-owned natural gas, electric, and water utility services, as well as the major intra-Alberta gas transmission system, to ensure that customers receive safe and reliable service at just and reasonable rates. [Emphasis added.]

61 The process by which the Board sets the rates is therefore central and deserves some attention in order to ascertain the validity of the City's first argument.

2.3.3.2 *Rate Setting*

62 Rate regulation serves several aims — sustainability, equity and efficiency — which underlie the reasoning as to how rates are fixed:

> . . . the regulated company must be able to finance its operations, and any required investment, so that it can continue to operate in the future. . . . Equity is related to the distribution of welfare among members of society. The objective of sustainability already implies that shareholders should not receive "too low" a return (and defines this in terms of the reward necessary to ensure continued investment in the utility), while equity implies that their returns should not be "too high".

(R. Green and M. Rodriguez Pardina, *Resetting Price Controls for Privatized Utilities: A Manual for Regulators* (1999), at p. 5)

63 These goals have resulted in an economic and social arrangement dubbed the "regulatory

les entreprises de services publics. Un régime de réglementation aussi vaste doit, pour être efficace, comprendre le droit de contrôler les réunions ou, pour reprendre l'expression du législateur, « l'union » des entreprises et installations existantes. Cela a sans aucun doute un rapport direct avec la fonction de fixation des tarifs qui constitue un des pouvoirs les plus importants attribués à la Commission. [Je souligne.]

Voici d'ailleurs comment la Commission décrit elle-même ses fonctions sur son site Internet (http://www.eub.gov.ab.ca/BBS/eubinfo/default.htm) :

> [TRADUCTION] La Commission réglemente l'exploitation sûre, responsable et efficiente des ressources énergétiques de l'Alberta — pétrole, gaz naturel, sables bitumineux, charbon et électricité — ainsi que les pipelines et les lignes de transport servant à l'acheminement vers les marchés. En ce qui a trait aux services publics, elle réglemente les tarifs des services de gaz naturel, d'électricité et d'eau appartenant au privé et le niveau de service y afférent, ainsi que les principaux réseaux de transport de gaz en Alberta, afin que les clients obtiennent des services sûrs et fiables à un prix juste et raisonnable. [Je souligne.]

Le processus par lequel la Commission fixe les tarifs est donc fondamental et son examen s'impose pour statuer sur la première prétention de la Ville.

2.3.3.2 *Établissement des tarifs*

La réglementation tarifaire a plusieurs objectifs — viabilité, équité et efficacité — qui expliquent le mode de fixation des tarifs :

> [TRADUCTION] . . . l'entreprise réglementée doit être en mesure de financer ses activités et tout investissement nécessaire à la poursuite de ses activités. [. . .] L'équité est liée à la redistribution de la richesse dans la société. L'objectif de la viabilité suppose déjà que les actionnaires ne doivent pas réaliser un « trop faible » rendement (défini comme la gratification requise pour assurer l'investissement continu dans l'entreprise), alors que celui de l'équité implique qu'ils ne doivent pas obtenir un rendement « trop élevé ».

(R. Green et M. Rodriguez Pardina, *Resetting Price Controls for Privatized Utilities : A Manual for Regulators* (1999), p. 5)

Ces objectifs sont à l'origine d'un arrangement économique et social appelé « pacte

compact", which ensures that all customers have access to the utility at a fair price — nothing more. As I will further explain, it does not transfer onto the customers any property right. Under the regulatory compact, the regulated utilities are given exclusive rights to sell their services within a specific area at rates that will provide companies the opportunity to earn a fair return for their investors. In return for this right of exclusivity, utilities assume a duty to adequately and reliably serve all customers in their determined territories, and are required to have their rates and certain operations regulated (see Black, at pp. 356-57; Milner, at p. 101; *Atco Ltd.*, at p. 576; *Northwestern Utilities Ltd. v. City of Edmonton*, [1929] S.C.R. 186 ("*Northwestern 1929*"), at pp. 192-93).

Therefore, when interpreting the broad powers of the Board, one cannot ignore this well-balanced regulatory arrangement which serves as a backdrop for contextual interpretation. The object of the statutes is to protect both the customer *and* the investor (Milner, at p. 101). The arrangement does not, however, cancel the private nature of the utility. In essence, the Board is responsible for maintaining a tariff that enhances the economic benefits to consumers and investors of the utility.

The Board derives its power to set rates from both the GUA (ss. 16, 17 and 36 to 45) and the PUBA (ss. 89 to 95). The Board is mandated to fix "just and reasonable . . . rates" (PUBA, s. 89(a); GUA, s. 36(a)). In the establishment of these rates, the Board is directed to "determine a rate base for the property of the owner" and "fix a fair return on the rate base" (GUA, s. 37(1)). This Court, in *Northwestern Utilities Ltd. v. City of Edmonton*, [1979] 1 S.C.R. 684 ("*Northwestern 1979*"), at p. 691, adopted the following description of the process:

> The PUB approves or fixes utility rates which are estimated to cover expenses plus yield the utility a fair return or profit. This function is generally performed in two phases. In Phase I the PUB determines the rate base, that is the amount of money which has been invested by the company in the property, plant and equipment plus an allowance for necessary working capital all of which must be determined as being necessary to

réglementaire » qui garantit à tous les clients l'accès au service public à un prix raisonnable, sans plus, et qui, je l'explique plus loin, ne transmet aucun droit de propriété aux clients. Le pacte réglementaire accorde en fait aux entreprises réglementées le droit exclusif de vendre leurs services dans une région donnée à des tarifs leur permettant de réaliser un juste rendement au bénéfice de leurs actionnaires. En contrepartie de ce monopole, elles ont l'obligation d'offrir un service adéquat et fiable à tous les clients d'un territoire donné et voient leurs tarifs et certaines de leurs activités assujettis à la réglementation (voir Black, p. 356-357; Milner, p. 101; *Atco Ltd.*, p. 576; *Northwestern Utilities Ltd. c. City of Edmonton*, [1929] R.C.S. 186 (« *Northwestern 1929* »), p. 192-193).

64 Par conséquent, lorsqu'il s'agit d'interpréter les vastes pouvoirs de la Commission, on ne peut faire abstraction de ce subtil compromis servant de toile de fond à l'interprétation contextuelle. L'objet de la législation est de protéger le client *et* l'investisseur (Milner, p. 101). Le pacte ne supprime pas le caractère privé de l'entreprise. La Commission a essentiellement pour mandat d'établir une tarification qui accroît les avantages financiers des consommateurs et des investisseurs.

65 Elle tient son pouvoir de fixer les tarifs à la fois de la GUA (art. 16 et 17 et art. 36 à 45) et de la PUBA (art. 89 à 95). Il lui incombe de fixer des [TRADUCTION] « tarifs [. . .] justes et raisonnables » (PUBA, al. 89a); GUA, al. 36a)). Pour le faire, elle doit [TRADUCTION] « établi[r] une base tarifaire pour les biens du propriétaire » et « fixe[r] un juste rendement par rapport à cette base tarifaire » (GUA, par. 37(1)). Dans *Northwestern Utilities Ltd. c. Ville d'Edmonton*, [1979] 1 R.C.S. 684 (« *Northwestern 1979* »), p. 691, notre Cour a décrit le processus comme suit :

> La PUB approuve ou fixe pour les services publics des tarifs destinés à couvrir les dépenses et à permettre à l'entreprise d'obtenir un taux de rendement ou profit convenable. Le processus s'accomplit en deux étapes. Dans la première étape, la PUB établit une base de tarification en calculant le montant des fonds investis par la compagnie en terrains, usines et équipements, plus le montant alloué au fonds de roulement, sommes dont

provide the utility service. The revenue required to pay all reasonable operating expenses plus provide a fair return to the utility on its rate base is also determined in Phase I. The total of the operating expenses plus the return is called the revenue requirement. In Phase II rates are set, which, under normal temperature conditions are expected to produce the estimates of "forecast revenue requirement". These rates will remain in effect until changed as the result of a further application or complaint or the Board's initiative. Also in Phase II existing interim rates may be confirmed or reduced and if reduced a refund is ordered.

(See also *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Decision No. E84113, October 12, 1984, at p. 23; *Re Union Gas Ltd. and Ontario Energy Board* (1983), 1 D.L.R. (4th) 698 (Ont. Div. Ct.), at pp. 701-2.)

66 Consequently, when determining the rate base, the Board is to give due consideration (GUA, s. 37(2)):

(a) to the cost of the property when first devoted to public use and to prudent acquisition cost to the owner of the gas utility, less depreciation, amortization or depletion in respect of each, and

(b) to necessary working capital.

67 The fact that the utility is given the opportunity to make a profit on its services and a fair return on its investment in its assets should not and cannot stop the utility from benefiting from the profits which follow the sale of assets. Neither is the utility protected from losses incurred from the sale of assets. In fact, the wording of the sections quoted above suggests that the ownership of the assets is clearly that of the utility; ownership of the asset and entitlement to profits or losses upon its realization are one and the same. The equity investor expects to receive the net revenues after all costs are paid, equal to the present value of original investment at the time of that investment. The disbursement of some portions of the residual amount of net revenue, by after-the-fact reallocation to rate-paying customers, undermines that investment process:

il faut établir la nécessité dans l'exploitation de l'entreprise. C'est également à cette première étape qu'est calculé le revenu nécessaire pour couvrir les dépenses d'exploitation raisonnables et procurer un rendement convenable sur la base de tarification. Le total des dépenses d'exploitation et du rendement donne un montant appelé le revenu nécessaire. Dans une deuxième étape, les tarifs sont établis de façon à pouvoir produire, dans des conditions météorologiques normales, « le revenu nécessaire prévu ». Ces tarifs restent en vigueur tant qu'ils ne sont pas modifiés à la suite d'une nouvelle requête ou d'une plainte, ou sur intervention de la Commission. C'est également à cette seconde étape que les tarifs provisoires sont confirmés ou réduits et, dans ce dernier cas, qu'un remboursement est ordonné.

(Voir également *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Décision nº E84113, 12 octobre 1984, p. 23; *Re Union Gas Ltd. and Ontario Energy Board* (1983), 1 D.L.R. (4th) 698 (C. div. Ont.), p. 701-702.)

Pour établir la base tarifaire, la Commission tient donc compte (GUA, par. 37(2)) :

[TRADUCTION]

a) du coût du bien lors de son affectation initiale à l'utilisation publique et de sa juste valeur d'acquisition pour le propriétaire du service de gaz, moins la dépréciation, l'amortissement et l'épuisement;

b) du capital nécessaire.

Le fait que l'on donne au service public la possibilité de tirer un profit de la prestation du service et de bénéficier d'un juste rendement de son actif ne peut ni ne devrait l'empêcher d'encaisser le bénéfice résultant de la vente d'un élément d'actif. L'entreprise n'est d'ailleurs pas non plus à l'abri de la perte pouvant en découler. Il ressort du libellé des dispositions précitées que les biens appartiennent à l'entreprise de services publics. Droit de propriété sur les biens et droit au profit ou à la perte lors de leur réalisation vont de pair. L'investisseur s'attend à toucher le produit net, une fois tous les frais payés, soit l'équivalent de la valeur actualisée de l'investissement initial. Le versement aux clients d'une partie du produit net restant, à l'issue d'une nouvelle répartition, sape le processus d'investissement : MacAvoy et Sidak, p. 244. À vrai dire, les

MacAvoy and Sidak, at p. 244. In fact, speculation would accrue even more often should the public utility, through its shareholders, not be the one to benefit from the possibility of a profit, as investors would expect to receive a larger premium for their funds through the only means left available, the return on their original investment. In addition, they would be less willing to accept any risk.

Thus, can it be said, as alleged by the City, that the customers have a property interest in the utility? Absolutely not: that cannot be so, as it would mean that fundamental principles of corporate law would be distorted. Through the rates, the customers pay an amount for the regulated service that equals the cost of the service and the necessary resources. They do not by their payment implicitly purchase the asset from the utility's investors. The payment does not incorporate acquiring ownership or control of the utility's assets. The ratepayer covers the cost of using the service, not the holding cost of the assets themselves: "A utility's customers are not its owners, for they are not residual claimants": MacAvoy and Sidak, at p. 245 (see also p. 237). Ratepayers have made no investment. Shareholders have and they assume all risks as the residual claimants to the utility's profit. Customers have only "the risk of a price change resulting from any (authorized) change in the cost of service. This change is determined only periodically in a tariff review by the regulator" (MacAvoy and Sidak, at p. 245).

In this regard, I agree with ATCO when it asserts in its factum, at para. 38:

> The property in question is as fully the private property of the owner of the utility as any other asset it owns. Deployment of the asset in utility service does not create or transfer any legal or equitable rights in that property for ratepayers. Absent any such interest, any taking such as ordered by the Board is confiscatory . . . .

Wittmann J.A., at the Court of Appeal, said it best when he stated:

> Consumers of utilities pay for a service, but by such payment, do not receive a proprietary right in the

opérations de spéculation seraient encore plus fréquentes si le service public et ses actionnaires ne touchaient pas le profit éventuel, car les investisseurs s'attendraient à obtenir une meilleure prime de la seule manière alors possible, le rendement de la mise de fonds initiale; en outre, ils seraient moins disposés à courir un risque.

68 La Ville a-t-elle raison alors de prétendre que les clients ont un droit de propriété sur le service public? Absolument pas. Sinon, les principes fondamentaux du droit des sociétés seraient dénaturés. En acquittant sa facture, le client paie pour le service réglementé un montant équivalant au coût du service et des ressources nécessaires. Il ne se porte pas implicitement acquéreur des biens des investisseurs. Le paiement n'emporte pas l'acquisition d'un droit de propriété ou de possession sur les biens. Le client acquitte le prix du service, à l'exclusion du coût de possession des biens eux-mêmes : [TRADUCTION] « Le client d'un service public n'en est pas le propriétaire puisqu'il n'a pas droit au reliquat des biens » : MacAvoy et Sidak, p. 245 (voir également p. 237). Le client n'a rien investi. Les actionnaires, eux, ont investi des fonds et assument tous les risques car ils touchent le profit restant. Le client court seulement le [TRADUCTION] « risque que le prix change par suite de la modification (autorisée) du coût du service, ce qui n'arrive que périodiquement lors de la révision des tarifs par l'organisme de réglementation » (MacAvoy et Sidak, p. 245).

69 Je suis d'accord avec ce qu'affirme ATCO à ce sujet au par. 38 de son mémoire :

> [TRADUCTION] Les biens en cause appartiennent au propriétaire du service public tout comme ses autres biens. Nul droit issu de la loi ou de l'equity n'est conféré ou transmis au client à l'égard d'un bien du fait de son affectation à un service public. Faute d'un tel droit, une appropriation, comme celle ordonnée par la Commission, a un effet confiscatoire . . .

Comme l'a si bien dit le juge Wittmann, de la Cour d'appel :

> [TRADUCTION] Le client d'un service public paie un service, mais n'obtient aucun droit de propriété sur les

assets of the utility company. Where the calculated rates represent the fee for the service provided in the relevant period of time, ratepayers do not gain equitable or legal rights to non-depreciable assets when they have paid only for the use of those assets. [Emphasis added; para. 64.]

I fully adopt this conclusion. The Board misdirected itself by confusing the interests of the customers in obtaining safe and efficient utility service with an interest in the underlying assets owned only by the utility. While the utility has been compensated for the services provided, the customers have provided no compensation for receiving the benefits of the subject property. The argument that assets purchased are reflected in the rate base should not cloud the issue of determining who is the appropriate owner and risk bearer. Assets are indeed considered in rate setting, as a factor, and utilities cannot sell an asset used in the service to create a profit and thereby restrict the quality or increase the price of service. Despite the consideration of utility assets in the rate-setting process, shareholders are the ones solely affected when the actual profits or losses of such a sale are realized; the utility absorbs losses and gains, increases and decreases in the value of assets, based on economic conditions and occasional unexpected technical difficulties, but continues to provide certainty in service both with regard to price and quality. There can be a default risk affecting ratepayers, but this does not make ratepayers residual claimants. While I do not wish to unduly rely on American jurisprudence, I would note that the leading U.S. case on this point is *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989), which relies on the same principle as was adopted in *Market St. Ry. Co. v. Railroad Commission of State of California*, 324 U.S. 548 (1945).

70 Furthermore, one has to recognize that utilities are not Crown entities, fraternal societies or cooperatives, or mutual companies, although they have a "public interest" aspect which is to supply the public with a necessary service (in the present case,

biens de cette entreprise. Lorsque le tarif établi correspond au prix du service pour la période considérée, le client n'acquiert à l'égard des biens non amortissables aucun droit fondé sur l'equity ou issu de la loi lorsqu'il n'a payé que pour l'utilisation de ces biens. [Je souligne; par. 64.]

Je suis entièrement d'accord. La Commission s'est méprise en confondant le droit des clients à un service sûr et efficace avec le droit sur les biens affectés à la prestation de ce service et dont l'entreprise est l'unique propriétaire. Alors que l'entreprise a été rémunérée pour le service fourni, les clients n'ont versé aucune contrepartie en échange du profit tiré de la vente des biens. L'argument voulant que les biens achetés soient pris en compte dans l'établissement de la base tarifaire ne doit pas embrouiller la question de savoir qui est le véritable titulaire du droit de propriété sur les biens et qui supporte les risques y afférents. Les biens comptent effectivement parmi les facteurs considérés pour fixer les tarifs, et un service public ne peut vendre un bien affecté à la prestation du service pour réaliser un profit et, ce faisant, diminuer la qualité du service ou majorer son prix. Même si les biens du service public sont pris en compte dans l'établissement de la base tarifaire, les actionnaires sont les seuls touchés lorsque la vente donne lieu à un profit ou à une perte. L'entreprise absorbe les pertes et les gains, l'appréciation ou la dépréciation des biens, eu égard à la conjoncture économique et aux défaillances techniques imprévues, mais elle continue de fournir un service fiable sur le plan de la qualité et du prix. Le client peut courir le risque que l'entreprise manque à ses obligations, mais cela ne lui donne pas droit au reliquat des biens. Sans m'appuyer indûment sur la jurisprudence américaine, je signale qu'aux États-Unis, l'arrêt de principe en la matière est *Duquesne Light Co. c. Barasch*, 488 U.S. 299 (1989), qui s'appuie sur le même principe que celui appliqué dans l'arrêt *Market St. Ry. Co. c. Railroad Commission of State of California*, 324 U.S. 548 (1945).

De plus, il faut reconnaître qu'une entreprise de services publics n'est pas une société d'État, une association d'assistance mutuelle, une coopérative ou une société mutuelle même si elle sert « l'intérêt public » en fournissant à la collectivité un service

the provision of natural gas). The capital invested is not provided by the public purse or by the customers; it is injected into the business by private parties who expect as large a return on the capital invested in the enterprise as they would receive if they were investing in other securities possessing equal features of attractiveness, stability and certainty (see *Northwestern 1929*, at p. 192). This prospect will necessarily include any gain or loss that is made if the company divests itself of some of its assets, i.e., land, buildings, etc.

From my discussion above regarding the property interest, the Board was in no position to proceed with an implicit refund by allocating to ratepayers the profits from the asset sale because it considered ratepayers had paid excessive rates for services in the past. As such, the City's first argument must fail. The Board was seeking to rectify what it perceived as a historic over-compensation to the utility by ratepayers. There is no power granted in the various statutes for the Board to execute such a refund in respect of an erroneous perception of past over-compensation. It is well established throughout the various provinces that utilities boards do not have the authority to retroactively change rates (*Northwestern 1979*, at p. 691; *Re Coseka Resources Ltd. and Saratoga Processing Co.* (1981), 126 D.L.R. (3d) 705 (Alta. C.A.), at p. 715, leave to appeal refused, [1981] 2 S.C.R. vii; *Re Dow Chemical Canada Inc.* (C.A.), at pp. 734-35). But more importantly, it cannot even be said that there was over-compensation: the rate-setting process is a speculative procedure in which both the ratepayers and the shareholders jointly carry their share of the risk related to the business of the utility (see MacAvoy and Sidak, at pp. 238-39).

2.3.3.3 *The Power to Attach Conditions*

As its second argument, the City submits that the power to allocate the proceeds from the sale of the utility's assets is necessarily incidental to the express powers conferred on the Board by the AEUBA, the GUA and the PUBA. It argues that the Board must necessarily have the power to allocate sale proceeds as part of its discretionary power to approve or refuse to approve a sale of assets. It

nécessaire (en l'occurrence, la distribution du gaz naturel). Son capital ne provient pas des pouvoirs publics ou des clients, mais d'investisseurs privés qui escomptent un rendement aussi élevé que celui offert par d'autres placements présentant les mêmes caractéristiques d'attractivité, de stabilité et de certitude (voir *Northwestern 1929*, p. 192). Les actionnaires s'attendent donc nécessairement à toucher le gain ou à subir la perte résultant de l'aliénation d'un élément d'actif de l'entreprise, comme un terrain ou un bâtiment.

71 Il appert de l'analyse qui précède portant sur le droit de propriété que la Commission ne pouvait effectuer un remboursement tacite en attribuant aux clients le profit tiré de la vente des biens au motif que les tarifs avaient été excessifs dans le passé. C'est pourquoi la première prétention de la Ville doit être rejetée. La Commission a tenté de remédier à une supposée rétribution excessive de l'entreprise de services publics par ses clients. Or, aucune des lois applicables ne lui confère le pouvoir d'effectuer un tel remboursement à partir d'une telle perception erronée. La jurisprudence des différentes provinces confirme que les organismes de réglementation n'ont pas le pouvoir de modifier les tarifs rétroactivement (*Northwestern 1979*, p. 691; *Re Coseka Resources Ltd. and Saratoga Processing Co.* (1981), 126 D.L.R. (3d) 705 (C.A. Alb.), p. 715, autorisation d'appel refusée, [1981] 2 R.C.S. vii; *Re Dow Chemical Canada Inc.* (C.A.), p. 734-735). Qui plus est, on ne peut même pas dire qu'il y a eu paiement excessif : la tarification est un processus conjectural où clients et actionnaires assument ensemble leur part du risque lié aux activités de l'entreprise de services publics (voir MacAvoy et Sidak, p. 238-239).

2.3.3.3 *Le pouvoir d'imposer des conditions*

72 La Ville soutient en second lieu que le pouvoir d'attribuer le produit de la vente des biens d'un service public est nécessairement accessoire aux pouvoirs exprès que confèrent à la Commission l'AEUBA, la GUA et la PUBA. Elle fait valoir que la Commission a nécessairement ce pouvoir lorsqu'elle exerce celui — discrétionnaire — d'autoriser ou non la vente d'éléments d'actifs, puisqu'elle

submits that this results from the fact that the Board is allowed to attach any condition to an order it makes approving such a sale. I disagree.

73 The City seems to assume that the doctrine of jurisdiction by necessary implication applies to "broadly drawn powers" as it does for "narrowly drawn powers"; this cannot be. The Ontario Energy Board in its decision in *Re Consumers' Gas Co.*, E.B.R.O. 410-II/411-II/412-II, March 23, 1987, at para. 4.73, enumerated the circumstances when the doctrine of jurisdiction by necessary implication may be applied:

* [when] the jurisdiction sought is necessary to accomplish the objectives of the legislative scheme and is essential to the Board fulfilling its mandate;
* [when] the enabling act fails to explicitly grant the power to accomplish the legislative objective;
* [when] the mandate of the Board is sufficiently broad to suggest a legislative intention to implicitly confer jurisdiction;
* [when] the jurisdiction sought must not be one which the Board has dealt with through use of expressly granted powers, thereby showing an absence of necessity; and
* [when] the Legislature did not address its mind to the issue and decide against conferring the power upon the Board.

(See also Brown, at p. 2-16.3.)

74 In light of the above, it is clear that the doctrine of jurisdiction by necessary implication will be of less help in the case of broadly drawn powers than for narrowly drawn ones. Broadly drawn powers will necessarily be limited to only what is rationally related to the purpose of the regulatory framework. This is explained by Professor Sullivan, at p. 228:

In practice, however, purposive analysis makes the powers conferred on administrative bodies almost infinitely elastic. Narrowly drawn powers can be understood to include "by necessary implication" all that is needed to enable the official or agency to achieve the

peut assortir de toute condition l'ordonnance autorisant la vente. Je ne suis pas d'accord.

La Ville semble tenir pour acquis que la doctrine de la compétence par déduction nécessaire s'applique tout autant aux pouvoirs « définis largement » qu'à ceux qui sont « biens circonscrits ». Ce ne saurait être le cas. Dans sa décision *Re Consumers' Gas Co.*, E.B.R.O. 410-II/411-II/412-II, 23 mars 1987, par. 4.73, la Commission de l'énergie de l'Ontario a énuméré les situations dans lesquelles s'applique la doctrine de la compétence par déduction nécessaire :

[TRADUCTION]

* la compétence alléguée est nécessaire à la réalisation des objectifs du régime législatif et essentielle à l'exécution du mandat de la Commission;
* la loi habilitante ne confère pas expressément le pouvoir de réaliser l'objectif législatif;
* le mandat de la Commission est suffisamment large pour donner à penser que l'intention du législateur était de lui conférer une compétence tacite;
* la Commission n'a pas à exercer la compétence alléguée en s'appuyant sur des pouvoirs expressément conférés, démontrant ainsi l'absence de nécessité;
* le législateur n'a pas envisagé la question et ne s'est pas prononcé contre l'octroi du pouvoir à la Commission.

(Voir également Brown, p. 2-16.3.)

Il est donc clair que la doctrine de la compétence par déduction nécessaire sera moins utile dans le cas de pouvoirs largement définis que dans celui de pouvoirs bien circonscrits. Les premiers seront nécessairement interprétés de manière à ne s'appliquer qu'à ce qui est rationnellement lié à l'objet de la réglementation. C'est ce qu'explique la professeure Sullivan, à la p. 228 :

[TRADUCTION] En pratique, toutefois, l'analyse téléologique rend les pouvoirs conférés aux organismes administratifs presque infiniment élastiques. Un pouvoir bien circonscrit peut englober, par « déduction nécessaire », tout ce qui est requis pour que le responsable

purpose for which the power was granted. Conversely, broadly drawn powers are understood to include only what is rationally related to the purpose of the power. In this way the scope of the power expands or contracts as needed, in keeping with the purpose. [Emphasis added.]

ou l'organisme puisse accomplir l'objet de son octroi. À l'inverse, on considère qu'un pouvoir largement défini vise uniquement ce qui est rationnellement lié à son objet. Il s'ensuit qu'un pouvoir a une portée qui augmente ou diminue au besoin, en fonction de son objet. [Je souligne.]

In the case at bar, s. 15 of the AEUBA, which allows the Board to impose additional conditions when making an order, appears at first glance to be a power having infinitely elastic scope. However, in my opinion, the attempt by the City to use it to augment the powers of the Board in s. 26(2) of the GUA must fail. The Court must construe s. 15(3) of the AEUBA in accordance with the purpose of s. 26(2).

75 En l'espèce, l'art. 15 de l'AEUBA, qui permet à la Commission d'imposer des conditions supplémentaires dans le cadre d'une ordonnance, paraît à première vue conférer un pouvoir dont la portée est infiniment élastique. J'estime cependant que la Ville ne saurait y avoir recours pour accroître les pouvoirs que le par. 26(2) de la GUA confère à la Commission. Notre Cour doit interpréter le par. 15(3) de l'AEUBA conformément à l'objet du par. 26(2).

MacAvoy and Sidak, in their article, at pp. 234-36, suggest three broad reasons for the requirement that a sale must be approved by the Board:

1. It prevents the utility from degrading the quality, or reducing the quantity, of the regulated service so as to harm consumers;

2. It ensures that the utility maximizes the aggregate economic benefits of its operations, and not merely the benefits flowing to some interest group or stakeholder; and

3. It specifically seeks to prevent favoritism toward investors.

76 Dans leur article, MacAvoy et Sidak avancent trois raisons principales d'exiger qu'une vente soit autorisée par la Commission (p. 234-236) :

1. éviter que l'entreprise de services publics ne diminue qualitativement ou quantitativement le service réglementé et ne cause de la sorte un préjudice aux clients;

2. garantir que l'entreprise maximisera l'ensemble des avantages financiers tirés de ses activités, et non seulement ceux destinés à certains groupes d'intérêt ou d'autres intéressés;

3. éviter précisément que les investisseurs ne soient favorisés.

Consequently, in order to impute jurisdiction to a regulatory body to allocate proceeds of a sale, there must be evidence that the exercise of that power is a practical necessity for the regulatory body to accomplish the objects prescribed by the legislature, something which is absent in this case (see *National Energy Board Act (Can.) (Re)*, [1986] 3 F.C. 275 (C.A.)). In order to meet these three goals, it is not necessary for the Board to have control over which party should benefit from the sale proceeds. The public interest component cannot be said to be sufficient to impute to the Board the power to allocate all the profits pursuant to the sale of assets. In fact, it is not necessary for the Board in

77 Par conséquent, pour qu'un organisme de réglementation ait le pouvoir d'attribuer le produit d'une vente, la preuve doit établir que ce pouvoir lui est nécessaire dans les faits pour atteindre les objectifs de la loi, ce qui n'est pas le cas en l'espèce (voir l'arrêt *Loi sur l'Office national de l'énergie (Can.) (Re)*, [1986] 3 C.F. 275 (C.A.)). Pour satisfaire aux trois exigences susmentionnées, il n'est pas nécessaire que la Commission détermine qui touchera le produit de la vente. Le volet intérêt public ne peut à lui seul lui conférer le pouvoir d'attribuer la totalité du profit tiré de la vente de biens. En fait, il n'est pas nécessaire à l'accomplissement de son mandat qu'elle puisse ordonner à l'entreprise de services

carrying out its mandate to order the utility to surrender the bulk of the proceeds from a sale of its property in order for that utility to obtain approval for a sale. The Board has other options within its jurisdiction which do not involve the appropriation of the sale proceeds, the most obvious one being to refuse to approve a sale that will, in the Board's view, affect the quality and/or quantity of the service offered by the utility or create additional operating costs for the future. This is not to say that the Board can never attach a condition to the approval of sale. For example, the Board could approve the sale of the assets on the condition that the utility company gives undertakings regarding the replacement of the assets and their profitability. It could also require as a condition that the utility reinvest part of the sale proceeds back into the company in order to maintain a modern operating system that achieves the optimal growth of the system.

78 In my view, allowing the Board to confiscate the net gain of the sale under the pretence of protecting rate-paying customers and acting in the "public interest" would be a serious misconception of the powers of the Board to approve a sale; to do so would completely disregard the economic rationale of rate setting, as I explained earlier in these reasons. Such an attempt by the Board to appropriate a utility's excess net revenues for ratepayers would be highly sophisticated opportunism and would, in the end, simply increase the utility's capital costs (MacAvoy and Sidak, at p. 246). At the risk of repeating myself, a public utility is first and foremost a private business venture which has as its goal the making of profits. This is not contrary to the legislative scheme, even though the regulatory compact modifies the normal principles of economics with various restrictions explicitly provided for in the various enabling statutes. None of the three statutes applicable here provides the Board with the power to allocate the proceeds of a sale and therefore affect the property interests of the public utility.

79 It is well established that potentially confiscatory legislative provision ought to be construed cautiously so as not to strip interested parties of their rights without the clear intention of the

publics de céder la plus grande partie du produit de la vente en contrepartie de l'autorisation accordée. La Commission dispose, dans les limites de sa compétence, d'autres moyens que l'appropriation du produit de la vente, le plus évident étant le refus d'autoriser une vente qui, à son avis, nuira à la qualité ou à la quantité des services offerts ou occasionnera des frais d'exploitation supplémentaires. Ce qui ne veut pas dire qu'elle ne peut jamais assujettir son autorisation à une condition. Par exemple, elle pourrait autoriser la vente à la condition que l'entreprise prenne des engagements en ce qui concerne le remplacement des biens en cause et leur rentabilité. Elle pourrait aussi exiger le réinvestissement d'une partie du produit de la vente dans l'entreprise afin de préserver un système d'exploitation moderne assurant une croissance optimale.

J'estime que permettre la confiscation du gain net tiré de la vente sous prétexte de protéger les clients et d'agir dans l'« intérêt public » c'est se méprendre grandement sur le pouvoir de la Commission d'autoriser ou non une vente et faire totalement abstraction des fondements économiques de la tarification exposés précédemment. S'approprier ainsi un produit net extraordinaire pour le compte des clients serait d'un opportunisme très poussé qui, en fin de compte, se traduirait par une hausse du coût du capital pour l'entreprise (MacAvoy et Sidak, p. 246). Au risque de me répéter, une entreprise de services publics est avant tout une entreprise privée dont l'objectif est de réaliser des profits. Cela n'est pas contraire au régime législatif, même si le pacte réglementaire modifie les principes économiques habituellement applicables, les lois habilitantes prévoyant explicitement différentes limitations. Aucune des trois lois pertinentes en l'espèce ne confère à la Commission le pouvoir d'attribuer le produit de la vente d'un bien et d'empiéter de la sorte sur le droit de propriété de l'entreprise de services publics.

Il est bien établi qu'une disposition législative susceptible d'avoir un effet confiscatoire doit être interprétée avec prudence afin de ne pas dépouiller les parties intéressées de leurs droits lorsque ce

legislation (see Sullivan, at pp. 400-403; Côté, at pp. 482-86; *Pacific National Investments Ltd. v. Victoria (City)*, [2000] 2 S.C.R. 919, 2000 SCC 64, at para. 26; *Leiriao v. Val-Bélair (Town)*, [1991] 3 S.C.R. 349, at p. 357; *Hongkong Bank of Canada v. Wheeler Holdings Ltd.*, [1993] 1 S.C.R. 167, at p. 197). Not only is the authority to attach a condition to allocate the proceeds of a sale to a particular party unnecessary for the Board to accomplish its role, but deciding otherwise would lead to the conclusion that a broadly drawn power can be interpreted so as to encroach on the economic freedom of the utility, depriving it of its rights. This would go against the above principles of interpretation.

If the Alberta legislature wishes to confer on ratepayers the economic benefits resulting from the sale of utility assets, it can expressly provide for this in the legislation, as was done by some states in the United States (e.g., Connecticut).

2.4 *Other Considerations*

Under the regulatory compact, customers are protected through the rate-setting process, under which the Board is required to make a well-balanced determination. The record shows that the City did not submit to the Board a general rate review application in response to ATCO's application requesting approval for the sale of the property at issue in this case. Nonetheless, if it chose to do so, this would not have stopped the Board, on its own initiative, from convening a hearing of the interested parties in order to modify and fix just and reasonable rates to give due consideration to any new economic data anticipated as a result of the sale (PUBA, s. 89(a); GUA, ss. 24, 36(a), 37(3), 40) (see Appendix).

2.5 *If Jurisdiction Had Been Found, Was the Board's Allocation Reasonable?*

In light of my conclusion with regard to jurisdiction, it is not necessary to determine whether

n'est pas l'intention manifeste du législateur (voir Sullivan, p. 400-403; Côté, p. 607-613; *Pacific National Investments Ltd. c. Victoria (Ville)*, [2000] 2 R.C.S. 919, 2000 CSC 64, par. 26; *Leiriao c. Val-Bélair (Ville)*, [1991] 3 R.C.S. 349, p. 357; *Banque Hongkong du Canada c. Wheeler Holdings Ltd.*, [1993] 1 R.C.S. 167, p. 197). Non seulement il n'est pas nécessaire, pour s'acquitter de sa mission, que la Commission ait le pouvoir d'attribuer à une partie le produit de la vente qu'elle autorise, mais toute conclusion contraire permettrait d'interpréter un pouvoir largement défini d'une façon qui empiète sur la liberté économique de l'entreprise de services publics, dépouillant cette dernière de ses droits, ce qui irait à l'encontre des principes d'interprétation susmentionnés.

80 Si l'assemblée législative albertaine souhaite que les clients bénéficient des avantages financiers découlant de la vente des biens d'un service public, elle peut le prévoir expressément dans la loi, à l'instar de certains États américains (le Connecticut, par exemple).

2.4 *Autres considérations*

81 Dans le cadre du pacte réglementaire, les clients sont protégés par la procédure d'établissement des tarifs à l'issue de laquelle la Commission doit rendre une décision pondérée. Il appert du dossier que la Ville n'a pas saisi la Commission d'une demande d'approbation du tarif général en réponse à celle présentée par ATCO afin d'obtenir l'autorisation de vendre des biens. Néanmoins, si elle l'avait fait, la Commission aurait pu, de son propre chef, convoquer les parties intéressées à une audience afin de fixer de nouveaux tarifs justes et raisonnables tenant dûment compte de la situation financière nouvelle devant résulter de la vente (PUBA, al. 89a); GUA, art. 24, al. 36a), par. 37(3), art. 40) (texte en annexe).

2.5 *À supposer que la Commission ait eu le pouvoir de répartir le produit de la vente, a-t-elle exercé ce pouvoir de manière raisonnable?*

82 Vu ma conclusion touchant à la compétence, il n'est pas nécessaire de déterminer si la Commission

the Board's exercise of discretion by allocating the sale proceeds as it did was reasonable. Nonetheless, given the reasons of my colleague Binnie J., I will address the issue very briefly. Had I not concluded that the Board lacked jurisdiction, my disposition of this case would have been the same, as I do not believe the Board met a reasonable standard when it exercised its power.

83 I am not certain how one could conclude that the Board's allocation was reasonable when it wrongly assumed that ratepayers had acquired a proprietary interest in the utility's assets because assets were a factor in the rate-setting process, and, moreover, when it explicitly concluded that no harm would ensue to customers from the sale of the asset. In my opinion, when reviewing the substance of the Board's decision, a court must conduct a two-step analysis: first, it must determine whether the order was warranted given the role of the Board to *protect the customers* (i.e., was the order *necessary in the public interest*?); and second, if the first question is answered in the affirmative, a court must then examine the validity of the Board's application of the *TransAlta Formula* (see para. 12 of these reasons), which refers to the difference between net book value and original cost, on the one hand, and appreciation in the value of the asset on the other. For the purposes of this analysis, I view the second step as a mathematical calculation and nothing more. I do not believe it provides the criteria which guides the Board to determine *if it should allocate* part of the sale proceeds to ratepayers. Rather, it merely guides the Board on *what to allocate and how to allocate it* (if it should do so in the first place). It is also interesting to note that there is no discussion of the fact that the book value used in the calculation must be referable solely to the financial statements of the utility.

84 In my view, as I have already stated, the power of the Board to allocate proceeds does not even arise in this case. Even by the Board's own reasoning, it should only exercise its discretion to act in the public interest when customers would be harmed

a exercé son pouvoir discrétionnaire de façon raisonnable en répartissant le produit de la vente comme elle l'a fait. Toutefois, vu les motifs de mon collègue le juge Binnie, je me penche très brièvement sur la question. Le règlement du pourvoi aurait été le même si j'avais conclu que la Commission avait ce pouvoir, car j'estime que la décision qu'elle a rendue sur son fondement ne satisfaisait pas à la norme de la raisonnabilité.

Je ne vois pas très bien comment on pourrait conclure que la répartition était raisonnable, la Commission ayant supposé à tort que les clients avaient acquis un droit de propriété sur les biens de l'entreprise du fait de la prise en compte de ceux-ci dans l'établissement des tarifs et ayant en outre conclu explicitement que la vente des biens ne causerait aucun préjudice aux clients. À mon avis, une cour de justice appelée à contrôler la décision au fond doit se livrer à une analyse en deux étapes. Premièrement, elle doit déterminer si l'ordonnance était justifiée au vu de l'obligation de la Commission de *protéger les clients* (c.-à-d. l'ordonnance était-elle *nécessaire dans l'intérêt public*?). Deuxièmement, dans l'affirmative, elle doit déterminer si la Commission a bien appliqué la *formule TransAlta* (voir le par. 12 des présents motifs), qui renvoie à la différence entre la valeur comptable nette des biens et leur coût historique, d'une part, et à l'appréciation des biens, d'autre part. Pour les besoins de l'analyse, je ne vois dans la deuxième étape qu'une opération mathématique, rien de plus. Je ne crois pas que la *formule TransAlta* oriente la décision de la Commission *d'attribuer ou non* une partie du produit de la vente aux clients. Elle ne préside qu'à la détermination de *ce qui sera attribué et des modalités d'attribution* (lorsqu'elle a décidé qu'il y avait lieu d'attribuer le produit de la vente). Il importe également de signaler que nul ne conteste que seule la valeur comptable figurant dans les états financiers de l'entreprise de services publics doit être utilisée pour le calcul.

Je le répète, la Commission n'était même pas justifiée, à mon sens, d'exercer le pouvoir d'attribuer le produit de la vente. Suivant son raisonnement même, elle ne doit exercer son pouvoir discrétionnaire d'agir dans l'intérêt public que lorsque les

or would face some risk of harm. But the Board was clear: there was no harm or risk of harm in the present situation:

> With the continuation of the same level of service at other locations and the acceptance by customers regarding the relocation, the Board is convinced there should be no impact on the level of service to customers as a result of the Sale. In any event, the Board considers that the service level to customers is a matter that can be addressed and remedied in a future proceeding if necessary.
>
> (Decision 2002-037, at para. 54)

After declaring that the customers would not, on balance, be harmed, the Board maintained that, on the basis of the evidence filed, there appeared to be a cost savings to the customers. There was no legitimate customer interest which could or needed to be protected by denying approval of the sale, or by making approval conditional on a particular allocation of the proceeds. Even if the Board had found a possible adverse effect arising from the sale, how could it allocate proceeds now based on an unquantified future potential loss? Moreover, in the absence of any factual basis to support it, I am also concerned with the presumption of bad faith on the part of ATCO that appears to underlie the Board's determination to protect the public from some possible future menace. In any case, as mentioned earlier in these reasons, this determination to protect the public interest is also difficult to reconcile with the actual power of the Board to prevent harm to ratepayers from occurring by simply refusing to approve the sale of a utility's asset. To that, I would add that the Board has considerable discretion in the setting of future rates in order to protect the public interest, as I have already stated.

In consequence, I am of the view that, in the present case, the Board did not identify any public interest which required protection and there was, therefore, nothing to trigger the exercise of the discretion to allocate the proceeds of sale. Hence, notwithstanding my conclusion on the first issue regarding the Board's jurisdiction, I would conclude

clients subiraient ou seraient susceptibles de subir un préjudice. Or sa conclusion à ce sujet est claire : aucun préjudice ou risque de préjudice n'était associé à l'opération projetée :

> [TRADUCTION] Comme les mêmes services seront offerts à partir d'autres installations, et vu l'acceptation de ce transfert par les clients, la Commission est convaincue que la vente ne devrait pas avoir de répercussions sur le niveau de service. Quoi qu'il en soit, elle considère que le niveau de service offert pourra au besoin faire l'objet d'un examen et d'une mesure corrective dans le cadre d'une procédure ultérieure.
>
> (Décision 2002-037, par. 54)

Après avoir déclaré que, tout bien considéré, les clients ne seraient pas lésés, la Commission a statué au vu des éléments de preuve présentés qu'ils réaliseraient apparemment des économies. Aucun droit légitime des clients ne pouvait ni ne devait être protégé par un refus d'autorisation ou un octroi assorti de la condition de répartir le produit de la vente d'une certaine manière. Même si la Commission avait conclu à la possibilité que la vente ait un effet préjudiciable, comment pouvait-elle, à ce stade, attribuer le produit de la vente en fonction d'une perte éventuelle indéterminée? La mauvaise foi présumée d'ATCO qui paraît sous-tendre la détermination de la Commission à protéger le public contre un risque éventuel, en l'absence de tout fondement factuel, me préoccupe également. De toute manière, je l'ai déjà dit, cette détermination à protéger l'intérêt public est également difficile à concilier avec le pouvoir exprès de la Commission de prévenir tout préjudice causé aux clients en refusant d'autoriser la vente des biens d'un service public. Je rappelle que la Commission jouit d'un pouvoir discrétionnaire considérable dans l'établissement des tarifs futurs afin de protéger l'intérêt public.

Par conséquent, je suis d'avis que la Commission n'a pas cerné d'intérêt public à protéger et qu'aucun élément ne justifiait donc l'exercice de son pouvoir discrétionnaire d'attribuer le produit de la vente. Indépendamment de ma conclusion au sujet de la compétence de la Commission, je conclus que sa décision d'exercer son pouvoir discrétionnaire

85

that the Board's decision to exercise its discretion to protect the public interest did not meet a reasonable standard.

3. Conclusion

86 This Court's role in this case has been one of interpreting the enabling statutes using the appropriate interpretive tools, i.e., context, legislative intention and objective. Going further than required by reading in *unnecessary* powers of an administrative agency under the guise of statutory interpretation is not consistent with the rules of statutory interpretation. It is particularly dangerous to adopt such an approach when property rights are at stake.

87 The Board did not have the jurisdiction to allocate the proceeds of the sale of the utility's asset; its decision did not meet the correctness standard. Thus, I would dismiss the City's appeal and allow ATCO's cross-appeal, both with costs. I would also set aside the Board's decision and refer the matter back to the Board to approve the sale of the property belonging to ATCO, recognizing that the proceeds of the sale belong to ATCO.

The reasons of McLachlin C.J. and Binnie and Fish JJ. were delivered by

88 BINNIE J. (dissenting) — The respondent ATCO Gas and Pipelines Ltd. ("ATCO") is part of a large entrepreneurial company that directly and through various subsidiaries operates both regulated businesses and unregulated businesses. The Alberta Energy and Utilities Board ("Board") believes it not to be in the public interest to encourage utility companies to mix together the two types of undertakings. In particular, the Board has adopted policies to discourage utilities from using their regulated businesses as a platform to engage in land speculation to increase their return on investment outside the regulatory framework. By awarding part of the profit to the utility (and its shareholders), the Board rewards utilities for diligence in divesting themselves of assets that are no longer productive, or that could be more productively employed elsewhere. However, by crediting part of the

de protéger l'intérêt public ne satisfaisait pas à la norme de la raisonnabilité.

3. Conclusion

Le rôle de notre Cour dans le présent pourvoi a été d'interpréter les lois habilitantes en tenant compte comme il se doit du contexte, de l'intention du législateur et de l'objectif législatif. Aller plus loin et conclure à l'issue d'une interprétation large que l'organisme administratif jouit de pouvoirs *non nécessaires* n'est pas conforme aux règles d'interprétation législative. Une telle approche est particulièrement dangereuse lorsqu'un droit de propriété est en jeu.

La Commission n'avait pas le pouvoir d'attribuer le produit de la vente d'un bien du service public; sa décision ne satisfaisait pas à la norme de la décision correcte. Par conséquent, je suis d'avis de rejeter le pourvoi de la Ville et d'accueillir le pourvoi incident d'ATCO, avec dépens dans les deux instances. Je suis également d'avis d'annuler la décision de la Commission et de lui renvoyer l'affaire en lui enjoignant d'autoriser la vente des biens d'ATCO et de reconnaître son droit au produit de la vente.

Version française des motifs de la juge en chef McLachlin et des juges Binnie et Fish rendus par

LE JUGE BINNIE (dissident) — L'intimée, ATCO Gas and Pipelines Ltd. (« ATCO »), fait partie d'une grande société qui, directement et par l'entremise de diverses filiales, exploite à la fois des entreprises réglementées et des entreprises non réglementées. L'Alberta Energy and Utilities Board (« Commission ») estime qu'il n'est pas dans l'intérêt public d'encourager les entreprises de services publics à jumeler leurs activités dans les deux secteurs. Plus particulièrement, elle a adopté des politiques afin de dissuader les entreprises de services publics de faire de leur secteur réglementé un lieu de spéculation foncière et d'augmenter ainsi le rendement de leurs investissements indépendamment du cadre réglementaire. En attribuant une partie du profit à l'entreprise de services publics (et à ses actionnaires), la Commission récompense la diligence avec laquelle elle se départit de biens qui ne sont

profit on the sale of such property to the utility's rate base (i.e. as a set-off to other costs), the Board seeks to dampen any incentive for utilities to skew decisions in their regulated business to favour such profit taking unduly. Such a balance, in the Board's view, is necessary in the interest of the public which allows ATCO to operate its utility business as a monopoly. In pursuit of this balance, the Board approved ATCO's application to sell land and warehousing facilities in downtown Calgary, but denied ATCO's application to keep for its shareholders the entire profit resulting from appreciation in the value of the land, whose cost of acquisition had formed part of the rate base on which gas rates had been calculated since 1922. The Board ordered the profit on the sale to be allocated one third to ATCO and two thirds as a credit to its cost base, thereby helping keep utility rates down, and to that extent benefiting ratepayers.

plus productifs ou qui pourraient l'être davantage s'ils étaient employés autrement. Toutefois, en portant une partie du profit au crédit de la base tarifaire de l'entreprise (c.-à-d. en la déduisant d'autres coûts), la Commission tente d'empêcher les entreprises de services publics de céder à la tentation d'infléchir les décisions afférentes à leurs activités réglementées pour favoriser la réalisation de profits indus. De son point de vue, un tel compromis est nécessaire dans l'intérêt du public, celui-ci conférant à ATCO un monopole dans un secteur d'activité. Dans la recherche de ce compromis, la Commission a autorisé ATCO à vendre un terrain et un entrepôt situés au centre-ville de Calgary, mais refusé qu'elle conserve, au bénéfice de ses actionnaires, la totalité du profit découlant de l'appréciation du terrain dont le coût d'acquisition était pris en compte, depuis 1922, pour la tarification du gaz naturel. La Commission a ordonné que le profit tiré de la vente soit attribué à raison d'un tiers à ATCO et que les deux tiers servent à réduire ses coûts, contribuant à contenir toute hausse des tarifs et favorisant ainsi la clientèle.

I have read with interest the reasons of my colleague Bastarache J. but, with respect, I do not agree with his conclusion. As will be seen, the Board has authority under s. 15(3) of the *Alberta Energy and Utilities Board Act*, R.S.A. 2000, c. A-17 ("AEUBA"), to impose on the sale "any additional conditions that the Board considers necessary in the public interest". Whether or not the conditions of approval imposed by the Board were necessary in the public interest was for the Board to decide. The Alberta Court of Appeal overruled the Board but, with respect, the Board is in a better position to assess necessity in this field for the protection of the public interest than either that court or this Court. I would allow the appeal and restore the Board's decision.

89 J'ai lu avec intérêt les motifs de mon collègue le juge Bastarache, mais, en toute déférence, je ne suis pas d'accord avec ses conclusions. Comme nous le verrons, le par. 15(3) de l'*Alberta Energy and Utilities Board Act*, R.S.A. 2000, ch. A-17 (« AEUBA »), confère à la Commission le pouvoir d'assujettir la vente aux [TRADUCTION] « conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public ». Il appartenait à la Commission de décider de la nécessité d'imposer des conditions dans l'intérêt public. La Cour d'appel de l'Alberta a infirmé la décision de la Commission. En toute déférence, j'estime que la Commission était mieux placée que la Cour d'appel ou que notre Cour pour juger de la nécessité de protéger l'intérêt public dans ce domaine. J'accueillerais le pourvoi et rétablirais la décision de la Commission.

I. Analysis

ATCO's argument boils down to the proposition announced at the outset of its factum:

I. Analyse

90 La thèse d'ATCO se résume à ce qu'elle affirme au début de son mémoire :

In the absence of any property right or interest and of any harm to the customers arising from the

[TRADUCTION] À défaut de tout droit de propriété et de tout préjudice causé à la clientèle par le

withdrawal from utility service, there was no proper ground for reaching into the pocket of the utility. In essence this case is about property rights.

(Respondent's factum, at para. 2)

91 For the reasons which follow I do not believe the case is about property rights. ATCO chose to make its investment in a regulated industry. The return on investment in the regulated gas industry is fixed by the Board, not the free market. In my view, the essential issue is whether the Alberta Court of Appeal was justified in limiting what the Board is allowed to "conside[r] necessary in the public interest".

A. *The Board's Statutory Authority*

92 The first question is one of jurisdiction. What gives the Board the authority to make the order ATCO complains about? The Board's answer is threefold. Section 22(1) of the *Gas Utilities Act*, R.S.A. 2000, c. G-5 ("GUA"), provides in part that "[t]he Board shall exercise a general supervision over all gas utilities, and the owners of them . . .". This, the Board says, gives it a broad jurisdiction to set policies that go beyond its specific powers in relation to specific applications, such as rate setting. Of more immediate pertinence, s. 26(2)(d)(i) of the same Act prohibits the regulated utility from selling, leasing or otherwise encumbering any of its property without the Board's approval. (To the same effect, see s. 101(2)(d)(i) of the *Public Utilities Board Act*, R.S.A. 2000, c. P-45.) It is common ground that this restraint on alienation of property applies to the proposed sale of ATCO's land and warehouse facilities in downtown Calgary, and that the Board could, in appropriate circumstances, simply have denied ATCO's application for approval of the sale. However, the Board was of the view to allow the sale subject to conditions. The Board ruled that the greater power (i.e. to deny the sale) must include the lesser (i.e. to allow the sale, subject to conditions):

In appropriate circumstances, the Board clearly has the power to prevent a utility from disposing of its property.

dessaisissement, rien ne justifiait qu'on puise dans les poches de l'entreprise. En fait, le présent pourvoi doit être réglé au regard du droit de propriété.

(Mémoire de l'intimée, par. 2)

Pour les motifs qui suivent, je ne crois pas que le litige ressortisse au droit de propriété. ATCO a choisi d'investir dans un secteur réglementé, celui de la distribution du gaz, où le rendement est établi par la Commission, et non par le marché. À mon avis, la question en litige est essentiellement de savoir si la Cour d'appel de l'Alberta était justifiée de restreindre les conditions que la Commission pouvait « juge[r] nécessaires dans l'intérêt public ».

A. *Les pouvoirs légaux de la Commission*

La première question qui se pose est celle de la compétence. D'où la Commission tient-elle le pouvoir de rendre l'ordonnance que conteste ATCO? La réponse de la Commission comporte trois volets. Le paragraphe 22(1) de la *Gas Utilities Act*, R.S.A. 2000, ch. G-5 (« GUA »), prévoit entre autres que [TRADUCTION] « [l]a Commission assure la surveillance générale des services de gaz et de leurs propriétaires . . . ». Selon la Commission, cette disposition lui confère le vaste pouvoir d'établir des politiques qui débordent le cadre du règlement de demandes au cas par cas (approbation de tarifs, etc.). Élément plus pertinent encore, le sous-al. 26(2)d)(i) de la même loi interdit à l'entreprise réglementée de vendre ses biens, de les louer ou de les grever par ailleurs sans l'autorisation de la Commission. (Voir dans le même sens le sous-al. 101(2)d)(i) de la *Public Utilities Board Act*, R.S.A. 2000, ch. P-45.) Tous conviennent que cette limitation s'applique à la vente projetée par ATCO du terrain et de l'entrepôt situés au centre-ville de Calgary et que si les circonstances l'avaient justifié, la Commission aurait pu simplement refuser son autorisation. En l'espèce, la Commission a décidé d'autoriser la vente et de l'assujettir à certaines conditions. Elle a statué que le pouvoir plus large de refuser d'autoriser la vente englobait celui, plus restreint, de l'autoriser en l'assujettissant à certaines conditions :

[TRADUCTION] Dans certaines circonstances, la Commission a clairement le pouvoir d'empêcher une

In the Board's view it also follows that the Board can approve a disposition subject to appropriate conditions to protect customer interests.

(Decision 2002-037, [2002] A.E.U.B.D. No. 52 (QL), at para. 47)

There is no need to rely on any such implicit power to impose conditions, however. As stated, the Board's explicit power to impose conditions is found in s. 15(3) of the AEUBA, which authorizes the Board to "make any further order and impose any additional conditions that the Board considers necessary in the public interest". In *Atco Ltd. v. Calgary Power Ltd.*, [1982] 2 S.C.R. 557, at p. 576, Estey J., for the majority, stated:

> It is evident from the powers accorded to the Board by the legislature in both statutes mentioned above that the legislature has given the Board a mandate of the widest proportions to safeguard the public interest in the nature and quality of the service provided to the community by the public utilities. [Emphasis added.]

The legislature says in s. 15(3) that the conditions are to be what *the Board* considers necessary. Of course, the discretionary power to impose conditions thus granted is not unlimited. It must be exercised in good faith for its intended purpose: *C.U.P.E. v. Ontario (Minister of Labour)*, [2003] 1 S.C.R. 539, 2003 SCC 29. ATCO says the Board overstepped even these generous limits. In ATCO's submission:

> Deployment of the asset in utility service does not create or transfer any legal or equitable rights in that property for ratepayers. Absent any such interest, any taking such as ordered by the Board is confiscatory . . . .

(Respondent's factum, at para. 38)

In my view, however, the issue before the Board was how much profit ATCO was entitled to earn on its investment in a regulated utility.

ATCO argues in the alternative that the Board engaged in impermissible "retroactive rate

entreprise de services publics de se départir d'un bien. Il s'ensuit donc qu'elle peut autoriser une aliénation et l'assortir de conditions susceptibles de bien protéger les intérêts du consommateur.

(Décision 2002-037, [2002] A.E.U.B.D. No. 52 (QL), par. 47)

Il n'est toutefois pas nécessaire qu'elle s'appuie sur un tel pouvoir implicite pour établir des conditions. Je le répète, le par. 15(3) de l'AEUBA confère explicitement à la Commission le pouvoir de [TRADUCTION] « rendre toute autre ordonnance et [d']imposer les conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public ». Dans *Atco Ltd. c. Calgary Power Ltd.*, [1982] 2 R.C.S. 557, p. 576, le juge Estey a dit au nom des juges majoritaires :

> Il ressort des pouvoirs que le législateur a accordé[s] à la Commission dans les deux lois mentionnées ci-dessus, qu'il a investi la Commission du mandat très général de veiller aux intérêts du public quant à la nature et à la qualité des services rendus à la collectivité par les entreprises de services publics. [Je souligne.]

Le paragraphe 15(3) dispose que les conditions fixées sont celles que *la Commission* juge nécessaires. Évidemment, son pouvoir discrétionnaire n'est pas illimité. Elle doit l'exercer de bonne foi et aux fins auxquelles il est conféré : *S.C.F.P. c. Ontario (Ministre du Travail)*, [2003] 1 R.C.S. 539, 2003 CSC 29. ATCO prétend que la Commission a même outrepassé un aussi large pouvoir. Voici un extrait de son mémoire :

> [TRADUCTION] Nul droit issu de la loi ou de l'equity n'est conféré ou transmis au client à l'égard d'un bien du fait de son affectation à un service public. Faute d'un tel droit, une appropriation, comme celle ordonnée par la Commission, a un effet confiscatoire . . .

(Mémoire de l'intimée, par. 38)

À mon avis, toutefois, la Commission devait déterminer la hauteur du profit qu'ATCO était admise à tirer de son investissement dans une entreprise réglementée.

Subsidiairement, ATCO soutient que la Commission s'est indûment livrée à une

making". But Alberta is an "original cost" jurisdiction, and no one suggests that the Board's original cost rate making during the 80-plus years this investment has been reflected in ATCO's ratebase was wrong. The Board proposed to apply a portion of the expected profit to future rate making. The effect of the order is prospective, not retroactive. Fixing the going-forward rate of return as well as general supervision of "all gas utilities, and the owners of them" were matters squarely within the Board's statutory mandate.

B. *The Board's Decision*

94 ATCO argues that the Board's decision should be seen as a stand-alone decision divorced from its rate-making responsibilities. However, I do not agree that the hearing under s. 26 of the GUA can be isolated in this way from the Board's general regulatory responsibilities. ATCO argues in its factum that

> the subject application by [ATCO] to the Board did not concern or relate to a rate application, and the Board was not engaged in fixing rates (if that could provide any justification, which is denied).
>
> (Respondent's factum, at para. 98)

95 It seems the Board proceeded with the s. 26 approval hearing separately from a rate setting hearing firstly because ATCO framed the proceeding in that way and secondly because this is the procedure approved by the Alberta Court of Appeal in *TransAlta Utilities Corp. v. Public Utilities Board (Alta.)* (1986), 68 A.R. 171. That case (which I will refer to as *TransAlta (1986)*) is a leading Alberta authority dealing with the allocation of the gain on the disposal of utility assets and the source of what is called the *TransAlta Formula* applied by the Board in this case. Kerans J.A. had this to say, at p. 174:

> I observe parenthetically that I now appreciate that it suits the convenience of everybody involved to resolve

« tarification rétroactive ». Or, l'Alberta a opté pour la tarification selon le « coût historique » et personne ne laisse entendre que, depuis plus de 80 ans, la Commission applique à tort cette méthode qui prend en compte l'investissement d'ATCO pour l'établissement de sa base tarifaire. La Commission a proposé de tenir compte d'une partie du profit escompté pour fixer les tarifs ultérieurs. L'ordonnance a un effet prospectif, et non rétroactif. La fixation du rendement futur et la surveillance générale [TRADUCTION] « des services de gaz et de leurs propriétaires » relevaient sans conteste du mandat légal de la Commission.

B. *La décision de la Commission*

ATCO soutient que la décision de la Commission doit être considérée isolément, sans égard aux attributions de l'organisme en matière de tarification. Toutefois, je ne crois pas que l'audience tenue pour l'application de l'art. 26 puisse être ainsi dissociée des attributions générales de la Commission à titre d'organisme de réglementation. Dans son mémoire, ATCO fait valoir ce qui suit :

> [TRADUCTION] . . . la demande d'[ATCO] n'avait rien à voir avec l'approbation de tarifs et la Commission n'était pas engagée dans un processus de tarification (à supposer que cela ait pu la justifier, ce qui est nié).
>
> (Mémoire de l'intimée, par. 98)

Il semble que la Commission ait entendu la demande d'autorisation fondée sur l'art. 26 indépendamment d'une demande d'approbation de tarifs en raison, premièrement, de la manière dont ATCO avait engagé l'instance et, deuxièmement, de l'approbation de cette démarche par la Cour d'appel de l'Alberta dans *TransAlta Utilities Corp. c. Public Utilities Board (Alta.)* (1986), 68 A.R. 171 (« *TransAlta (1986)* »). Il s'agit de l'arrêt de principe albertain en ce qui concerne l'attribution du profit réalisé lors de l'aliénation d'un bien affecté à un service public, et la Cour d'appel y a énoncé la *formule TransAlta* que la Commission a appliquée en l'espèce. Voici ce qu'a dit le juge Kerans à ce sujet (p. 174) :

> [TRADUCTION] Je signale en passant que je comprends maintenant que toutes les parties ont intérêt à ce que

issues of this sort, if possible, before a general rate hearing so as to lessen the burden on that already complex procedure.

les questions de cette nature soient, si possible, résolues avant l'audition de la demande générale de majoration tarifaire de manière à ne pas alourdir cette procédure déjà complexe.

Given this encouragement from the Alberta Court of Appeal, I would place little significance on ATCO's procedural point. As will be seen, the Board's ruling is directly tied into the setting of general rates because two thirds of the profit is taken into account as an offset to ATCO's costs from which its revenue requirement is ultimately derived. As stated, ATCO's profit on the sale of the Calgary property will be a current (not historical) receipt and, if the Board has its way, two thirds of it will be applied to future (not retroactive) rate making.

96 Fort de ces propos de la Cour d'appel de l'Alberta, j'accorderais peu d'importance à l'argument procédural d'ATCO. Nous le verrons, la décision de la Commission est directement liée à la tarification générale, les deux tiers du profit étant déduits des coûts à partir desquels sont ultimement déterminés les besoins en revenus d'ATCO. Je l'ai déjà dit, le profit tiré de la vente des biens d'ATCO situés à Calgary constituera une rentrée courante (et non historique), et si la décision de la Commission est confirmée, les deux tiers du profit tiré de l'opération seront pris en compte pour la tarification ultérieure (et non de manière rétroactive).

The s. 26 hearing proceeded in two phases. The Board first determined that it would not deny its approval to the proposed sale as it met a "no-harm test" devised over the years by Board practice (it is not to be found in the statutes) (Decision 2001-78). However, the Board linked its approval to subsequent consideration of the financial ramifications, as the Board itself noted:

97 L'audience tenue pour l'application de l'art. 26 s'est déroulée en deux étapes. La Commission a d'abord décidé qu'elle ne refusait pas d'autoriser la vente projetée vu l'« absence de préjudice », un critère qu'elle avait élaboré au fil des ans, mais qui n'était pas prévu dans les lois (décision 2001-78). Cependant, elle a lié son autorisation à l'examen subséquent des conséquences financières. Comme elle l'a elle-même fait remarquer :

> The Board approved the Sale in Decision 2001-78 based on evidence that customers did not object to the Sale [and] would not suffer a reduction in services nor would they be exposed to the risk of financial harm as a result of the Sale *that could not be examined in a future proceeding*. On that basis the Board determined that the no-harm test had been satisfied and that the Sale could proceed. [Underlining and italics added.]
>
> (Decision 2002-037, at para. 13)

> [TRADUCTION] Dans la décision 2001-78, la Commission a autorisé la vente parce qu'il avait été établi que les clients ne s'opposaient pas à l'opération, qu'ils ne subiraient pas une diminution de service et que la vente ne risquait pas de leur infliger un préjudice financier *qui ne pourrait faire l'objet d'un examen dans le cadre d'une procédure ultérieure*. Elle a donc conclu à l'absence de préjudice et décidé que la vente pouvait avoir lieu. [Soulignements et italiques ajoutés.]
>
> (Décision 2002-037, par. 13)

In effect, ATCO ignores the italicized words. It argues that the Board was *functus* after the first phase of its hearing. However, ATCO itself had agreed to the two-phase procedure, and indeed the second phase was devoted to ATCO's own application for an allocation of the profits on the sale.

98 ATCO fait abstraction de ce qui figure en italique dans cet extrait. Elle soutient que la Commission était *functus officio* après la première étape de l'audience. Or, elle avait elle-même consenti au déroulement de la procédure en deux étapes, et la deuxième partie de l'audience a effectivement été consacrée à sa demande d'attribution du profit tiré de la vente.

99 In the second phase of the s. 26 approval hearing, the Board allocated one third of the net gain to ATCO and two thirds to the rate base (which would benefit ratepayers). The Board spelled out why it considered these conditions to be necessary in the public interest. The Board explained that it was necessary to balance the interests of both shareholders and ratepayers within the framework of what it called "the regulatory compact" (Decision 2002-037, at para. 44). In the Board's view:

(a) there ought to be a balancing of the interests of the ratepayers and the owners of the utility;

(b) decisions made about the utility should be driven by both parties' interests;

(c) to award the entire gain to the ratepayers would deny the utility an incentive to increase its efficiency and reduce its costs; and

(d) to award the entire gain to the utility might encourage speculation in non-depreciable property or motivate the utility to identify and dispose of properties which have appreciated for reasons other than the best interest of the regulated business.

100 For purposes of this appeal, it is important to set out the Board's policy reasons in its own words:

> To award the entire net gain on the land and buildings to the customers, while beneficial to the customers, could establish an environment that may deter the process wherein the company continually assesses its operation to identify, evaluate, and select options that continually increase efficiency and reduce costs.
>
> Conversely, to award the entire net gain to the company may establish an environment where a regulated utility company might be moved to speculate in non-depreciable property or result in the company being motivated to identify and sell existing properties where appreciation has already occurred.
>
> The Board believes that some method of balancing both parties' interests will result in optimization

Au cours de la deuxième étape de l'audition de la demande fondée sur l'art. 26, la Commission a attribué un tiers du profit net à ATCO et deux tiers à la base tarifaire (au bénéfice des clients). Elle a exposé les raisons pour lesquelles elle jugeait cette répartition nécessaire à la protection de l'intérêt public. Elle a expliqué qu'il fallait mettre en balance les intérêts des actionnaires et ceux des clients dans le cadre de ce qu'elle a appelé [TRADUCTION] « le pacte réglementaire » (décision 2002-037, par. 44). Selon la Commission :

a) il faut mettre en balance les intérêts des clients et ceux des propriétaires de l'entreprise de services publics;

b) les décisions visant l'entreprise doivent tenir compte des intérêts des deux parties;

c) attribuer aux clients la totalité du profit tiré de la vente n'inciterait pas l'entreprise à accroître son efficacité et à réduire ses coûts;

d) en attribuer la totalité à l'entreprise pourrait encourager la spéculation à l'égard de biens non amortissables ou l'identification des biens dont la valeur s'est accrue et leur aliénation pour des motifs étrangers à l'intérêt véritable de l'entreprise réglementée.

Pour les besoins du présent pourvoi, il importe de rappeler les considérations de principe invoquées par la Commission :

> [TRADUCTION] Il serait avantageux pour les clients de leur attribuer la totalité du profit net tiré de la vente du terrain et des bâtiments, mais cela pourrait dissuader la société de soumettre son fonctionnement à une analyse continue afin de trouver des moyens d'améliorer son rendement et de réduire ses coûts de manière constante.
>
> À l'inverse, attribuer à l'entreprise réglementée la totalité du profit net pourrait encourager la spéculation à l'égard de biens non amortissables ou l'identification des biens dont la valeur s'est déjà accrue et leur aliénation.
>
> La Commission croit qu'une certaine mise en balance des intérêts des deux parties permettra la

of business objectives for both the customer and the company. Therefore, the Board considers that sharing of the net gain on the sale of the land and buildings collectively in accordance with the TransAlta Formula is equitable in the circumstances of this application and is consistent with past Board decisions. [Emphasis added; paras. 112-14.]

The Court was advised that the two-third share allocated to ratepayers would be included in ATCO's rate calculation to set off against the costs included in the rate base and amortized over a number of years.

C. *Standard of Review*

The Court's modern approach to this vexed question was recently set out by McLachlin C.J. in *Dr. Q v. College of Physicians and Surgeons of British Columbia*, [2003] 1 S.C.R. 226, 2003 SCC 19, at para. 26:

> In the pragmatic and functional approach, the standard of review is determined by considering four contextual factors — the presence or absence of a privative clause or statutory right of appeal; the expertise of the tribunal relative to that of the reviewing court on the issue in question; the purposes of the legislation and the provision in particular; and, the nature of the question — law, fact, or mixed law and fact. The factors may overlap. The overall aim is to discern legislative intent, keeping in mind the constitutional role of the courts in maintaining the rule of law.

I do not propose to cover the ground already set out in the reasons of my colleague Bastarache J. We agree that the standard of review on matters of jurisdiction is correctness. We also agree that the Board's *exercise* of its jurisdiction calls for greater judicial deference. Appeals from the Board are limited to questions of law or jurisdiction. The Board knows a great deal more than the courts about gas utilities, and what limits it is necessary to impose "in the public interest" on their dealings with assets whose cost is included in the rate base. Moreover, it is difficult to think of a broader discretion than that conferred on the Board to "impose any additional conditions that the Board considers necessary in the public interest" (s. 15(3)(d) of the AEUBA).

réalisation optimale des objectifs de l'entreprise dans son propre intérêt et dans celui de ses clients. Par conséquent, elle estime équitable en l'espèce et conforme à ses décisions antérieures de partager selon la formule TransAlta le profit net tiré de la vente du terrain et des bâtiments. [Je souligne; par. 112-114.]

101 On a informé notre Cour que les deux tiers du profit attribués aux clients seraient déduits des coûts considérés pour l'établissement de la base tarifaire d'ATCO, puis amortis sur un certain nombre d'années.

C. *La norme de contrôle*

102 L'approche actuelle de notre Cour à l'égard de cette question épineuse a récemment été précisée par la juge en chef McLachlin dans l'arrêt *Dr Q c. College of Physicians and Surgeons of British Columbia*, [2003] 1 R.C.S. 226, 2003 CSC 19, par. 26 :

> Selon l'analyse pragmatique et fonctionnelle, la norme de contrôle est déterminée en fonction de quatre facteurs contextuels — la présence ou l'absence dans la loi d'une clause privative ou d'un droit d'appel; l'expertise du tribunal relativement à celle de la cour de révision sur la question en litige; l'objet de la loi et de la disposition particulière; la nature de la question — de droit, de fait ou mixte de fait et de droit. Les facteurs peuvent se chevaucher. L'objectif global est de cerner l'intention du législateur, sans perdre de vue le rôle constitutionnel des tribunaux judiciaires dans le maintien de la légalité.

103 Je n'entends pas reprendre les propos de mon collègue le juge Bastarache à ce sujet. Nous convenons que la norme applicable en matière de compétence est celle de la décision correcte. Nous convenons également qu'en ce qui a trait à l'*exercice* de sa compétence par la Commission, une déférence accrue s'impose. Il ne peut être interjeté appel d'une décision de la Commission que sur une question de droit ou de compétence. La Commission en sait bien davantage qu'une cour de justice sur les services de gaz et les limites qui doivent leur être imposées « dans l'intérêt public » lorsqu'ils effectuent des opérations relatives à des biens dont le coût est inclus dans la base tarifaire. De plus, il est difficile d'imaginer un pouvoir discrétionnaire plus vaste que celui

The identification of a subjective discretion in the decision maker ("the Board considers necessary"), the expertise of that decision maker and the nature of the decision to be made ("in the public interest"), in my view, call for the most deferential standard, patent unreasonableness.

104 As to the phrase "the Board considers necessary", Martland J. stated in *Calgary Power Ltd. v. Copithorne*, [1959] S.C.R. 24, at p. 34:

> The question as to whether or not the respondent's lands were "necessary" is not one to be determined by the Courts in this case. The question is whether the Minister "deemed" them to be necessary.

See also D. J. M. Brown and J. M. Evans, *Judicial Review of Administrative Action in Canada* (loose-leaf ed.), vol. 1, at para. 14:2622: "'*Objective' and 'Subjective' Grants of Discretion*".

105 The expert qualifications of a regulatory Board are of "utmost importance in determining the intention of the legislator with respect to the degree of deference to be shown to a tribunal's decision in the absence of a full privative clause", as stated by Sopinka J. in *United Brotherhood of Carpenters and Joiners of America, Local 579 v. Bradco Construction Ltd.*, [1993] 2 S.C.R. 316, at p. 335. He continued:

> Even where the tribunal's enabling statute provides explicitly for appellate review, as was the case in *Bell Canada* [*v. Canada (Canadian Radio-Television and Telecommunications Commission)*, [1989] 1 S.C.R. 1722], it has been stressed that deference should be shown by the appellate tribunal to the opinions of the specialized lower tribunal on matters squarely within its jurisdiction.
>
> (This *dictum* was cited with approval in *Pezim v. British Columbia (Superintendent of Brokers)*, [1994] 2 S.C.R. 557, at p. 592.)

— conféré à la Commission — d'[TRADUCTION] « imposer les conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public » (al. 15(3)d) de l'AEUBA). L'élément subjectif de ce pouvoir (« qu'elle juge nécessaires »), l'expertise du décideur et la nature de la décision (« dans l'intérêt public ») appellent à mon avis la plus grande déférence et l'application de la norme de la décision manifestement déraisonnable.

En ce qui a trait à l'élément « qu'elle juge nécessaires », le juge Martland a dit ce qui suit dans l'arrêt *Calgary Power Ltd. c. Copithorne*, [1959] R.C.S. 24, p. 34 :

> [TRADUCTION] En l'espèce, il n'appartient pas à une cour de justice de déterminer si les terrains de l'intimé étaient ou non « nécessaires », mais bien si le ministre a « estimé » qu'ils l'étaient.

Voir également D. J. M. Brown et J. M. Evans, *Judicial Review of Administrative Action in Canada* (éd. feuilles mobiles), vol. 1, par. 14:2622 : « *"Objective" and "Subjective" Grants of Discretion* ».

Comme l'a dit le juge Sopinka dans l'arrêt *Fraternité unie des charpentiers et menuisiers d'Amérique, section locale 579 c. Bradco Construction Ltd.*, [1993] 2 R.C.S. 316, p. 335, l'expertise que possède un organisme de réglementation est « de la plus haute importance pour ce qui est de déterminer l'intention du législateur quant au degré de retenue dont il faut faire preuve à l'égard de la décision d'un tribunal en l'absence d'une clause privative intégrale ». Il a ajouté :

> Même lorsque la loi habilitante du tribunal prévoit expressément l'examen par voie d'appel, comme c'était le cas dans l'affaire *Bell Canada* [*c. Canada (Conseil de la radiodiffusion et des télécommunications canadiennes)*, [1989] 1 R.C.S. 1722], on a souligné qu'il y avait lieu pour le tribunal d'appel de faire preuve de retenue envers les opinions que le tribunal spécialisé de juridiction inférieure avait exprimées sur des questions relevant directement de sa compétence.
>
> (Cette opinion incidente a été citée avec approbation dans l'arrêt *Pezim c. Colombie-Britannique (Superintendent of Brokers)*, [1994] 2 R.C.S. 557, p. 592.)

A regulatory power to be exercised "in the public interest" necessarily involves accommodation of conflicting economic interests. It has long been recognized that what is "in the public interest" is not really a question of law or fact but is an opinion. In *TransAlta (1986)*, the Alberta Court of Appeal (at para. 24) drew a parallel between the scope of the words "public interest" and the well-known phrase "public convenience and necessity" in its citation of *Memorial Gardens Association (Canada) Ltd. v. Colwood Cemetery Co.*, [1958] S.C.R. 353, where this Court stated, at p. 357:

> [T]he question whether public convenience and necessity requires a certain action is not one of fact. It is predominantly the formulation of an opinion. Facts must, of course, be established to justify a decision by the Commission but that decision is one which cannot be made without a substantial exercise of administrative discretion. In delegating this administrative discretion to the Commission the Legislature has delegated to that body the responsibility of deciding, in the public interest . . . . [Emphasis added.]

This passage reiterated the *dictum* of Rand J. in *Union Gas Co. of Canada Ltd. v. Sydenham Gas and Petroleum Co.*, [1957] S.C.R. 185, at p. 190:

> It was argued, and it seems to have been the view of the Court, that the determination of public convenience and necessity was itself a question of fact, but with that I am unable to agree: it is not an objective existence to be ascertained; the determination is the formulation of an opinion, in this case, the opinion of the Board and of the Board only. [Emphasis added.]

Of course even such a broad power is not untrammelled. But to say that such a power is capable of abuse does not lead to the conclusion that it should be truncated. I agree on this point with Reid J. (co-author of R. F. Reid and H. David, *Administrative Law and Practice* (2nd ed. 1978), and co-editor of P. Anisman and R. F. Reid, *Administrative Law Issues and Practice* (1995)), who wrote in *Re C.T.C. Dealer Holdings Ltd. and Ontario Securities Commission* (1987), 59 O.R. (2d) 79 (Div. Ct.), in relation to the powers of the Ontario Securities Commission, at p. 97:

106 L'exercice d'un pouvoir de réglementation « dans l'intérêt public » exige nécessairement la conciliation d'intérêts économiques divergents. Il est depuis longtemps établi que la question de savoir ce qui est « dans l'intérêt public » n'est pas véritablement une question de droit ou de fait, mais relève plutôt de l'opinion. Dans *TransAlta (1986)*, la Cour d'appel de l'Alberta a fait (au par. 24) un parallèle entre la portée des mots « intérêt public » et celle de l'expression bien connue « la commodité et les besoins du public » en citant l'arrêt *Memorial Gardens Association (Canada) Ltd. c. Colwood Cemetery Co.*, [1958] R.C.S. 353, où notre Cour avait dit ce qui suit à la p. 357 :

> [TRADUCTION] [L]a question de savoir si la commodité et les besoins du public nécessitent l'accomplissement de certains actes n'est pas une question de fait. C'est avant tout l'expression d'une opinion. Il faut évidemment que la décision de la Commission se fonde sur des faits mis en preuve, mais cette décision ne peut être prise sans que la discrétion administrative y joue un rôle important. En conférant à la Commission ce pouvoir discrétionnaire, la Législature a délégué à cet organisme la responsabilité de décider, dans l'intérêt du public . . . [Je souligne.]

107 Dans cet extrait, notre Cour reprenait l'opinion incidente du juge Rand dans l'arrêt *Union Gas Co. of Canada Ltd. c. Sydenham Gas and Petroleum Co.*, [1957] R.C.S. 185, p. 190 :

> [TRADUCTION] On a prétendu, et la Cour a semblé d'accord, que l'appréciation de la commodité et des besoins du public est elle-même une question de fait, mais je ne puis souscrire à cette opinion : il ne s'agit pas de déterminer si objectivement telle situation existe. La décision consiste à exprimer une opinion, en l'espèce, l'opinion du Comité et du Comité seulement. [Je souligne.]

108 Évidemment, même un pouvoir aussi vaste n'est pas absolu. Mais reconnaître qu'il puisse faire l'objet d'abus n'implique pas qu'il doive être restreint. Je suis d'accord sur ce point avec l'avis exprimé par le juge Reid (coauteur de R. F. Reid et H. David, *Administrative Law and Practice* (2e éd. 1978), et coéditeur de P. Anisman et R. F. Reid, *Administrative Law Issues and Practice* (1995)), dans la décision *Re C.T.C. Dealer Holdings Ltd. and Ontario Securities Commission* (1987), 59 O.R. (2d) 79 (C. div.), p. 97, au sujet des pouvoirs de la Commission des valeurs mobilières de l'Ontario :

. . . when the Commission has acted *bona fide*, with an obvious and honest concern for the public interest, and with evidence to support its opinion, the prospect that the breadth of its discretion might someday tempt it to place itself above the law by misusing that discretion is not something that makes the existence of the discretion bad *per se*, and requires the decision to be struck down.

(The *C.T.C. Dealer Holdings* decision was referred to with apparent approval by this Court in *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, [2001] 2 S.C.R. 132, 2001 SCC 37, at para. 42.)

109 "Patent unreasonableness" is a highly deferential standard:

A correctness approach means that there is only one proper answer. A patently unreasonable one means that there could have been many appropriate answers, but not the one reached by the decision maker.

(*C.U.P.E.*, at para. 164)

110 Having said all that, in my view nothing much turns on the result on whether the proper standard in that regard is patent unreasonableness (as I view it) or simple reasonableness (as my colleague sees it). As will be seen, the Board's response is well within the range of established regulatory opinions. Hence, even if the Board's conditions were subject to the less deferential standard, I would find no cause for the Court to interfere.

D. *Did the Board Have Jurisdiction to Impose the Conditions It Did on the Approval Order "In the Public Interest"?*

111 ATCO says the Board had no jurisdiction to impose conditions that are "confiscatory". Framing the question in this way, however, assumes the point in issue. The correct point of departure is not to assume that ATCO is entitled to the net gain and then ask if the Board can confiscate it. ATCO's investment of $83,000 was added in increments to its regulatory cost base as the land was acquired from

[TRADUCTION] . . . lorsque la Commission a agi de bonne foi en se souciant clairement et véritablement de l'intérêt public et en fondant son opinion sur des éléments de preuve, le risque que l'étendue de son pouvoir discrétionnaire puisse un jour l'inciter à l'exercer abusivement et à se placer ainsi au-dessus de la loi ne fait pas de l'existence de ce pouvoir une mauvaise chose en soi et n'exige pas l'annulation de la décision de la Commission.

(Notre Cour a fait mention, apparemment avec approbation, de la décision *C.T.C. Dealer Holdings* dans l'arrêt *Comité pour le traitement égal des actionnaires minoritaires de la Société Asbestos ltée c. Ontario (Commission des valeurs mobilières)*, [2001] 2 R.C.S. 132, 2001 CSC 37, par. 42.)

La norme du « manifestement déraisonnable » appelle un degré élevé de déférence judiciaire :

La méthode de la décision correcte signifie qu'il n'y a qu'une seule réponse appropriée. La méthode du caractère manifestement déraisonnable signifie que de nombreuses réponses appropriées étaient possibles, sauf celle donnée par le décideur.

(*S.C.F.P.*, par. 164)

Cela dit, il importe peu à mon sens que la norme applicable soit celle du manifestement déraisonnable (comme je le pense) ou celle du raisonnable *simpliciter* (comme le croit mon collègue). Nous le verrons, la décision de la Commission se situe dans les limites des opinions exprimées par les organismes de réglementation. Même si une norme moins déférente s'appliquait aux conditions imposées par la Commission, je ne verrais aucune raison d'intervenir.

D. *La Commission avait-elle le pouvoir d'assortir son autorisation des conditions en cause « dans l'intérêt public »?*

ATCO prétend que la Commission n'avait pas le pouvoir d'imposer des conditions ayant un effet « confiscatoire ». Or, en s'exprimant ainsi, elle présume de la question en litige. La bonne démarche n'est pas de supposer qu'ATCO avait droit au profit net tiré de la vente, puis de se demander si la Commission pouvait le confisquer. L'investissement de 83 000 $ d'ATCO a graduellement été pris en

time to time between 1922 and 1965. It is in the nature of a regulated industry that the question of what is a just and equitable return is determined by a board and not by the vagaries of the speculative property market.

I do not think the legal debate is assisted by talk of "confiscation". ATCO is prohibited by statute from disposing of the asset without Board approval, and the Board has statutory authority to impose conditions on its approval. The issue thus necessarily turns not on the *existence* of the jurisdiction but on the *exercise* of the Board's jurisdiction to impose the conditions that it did, and in particular to impose a shared allocation of the net gain.

E. *Did the Board Improperly Exercise the Jurisdiction It Possessed to Impose Conditions the Board Considered "Necessary in the Public Interest"?*

There is no doubt that there are many approaches to "the public interest". Which approach the Board adopts is largely (and inherently) a matter of opinion and discretion. While the statutory framework of utilities regulation varies from jurisdiction to jurisdiction, and practice in the United States must be read in light of the constitutional protection of property rights in that country, nevertheless Alberta's grant of authority to its Board is more generous than most. ATCO concedes that its "property" claim would have to give way to a contrary legislative intent, but ATCO says such intent cannot be found in the statutes.

Most if not all regulators face the problem of how to allocate gains on property whose original cost is included in the rate base but is no longer required to provide the service. There is a wealth of regulatory experience in many jurisdictions that the Board is entitled to (and does) have regard to in formulating its policies. Striking the correct balance in the allocation of gains between ratepayers

compte dans sa base tarifaire réglementaire puisque l'acquisition du terrain s'est échelonnée de 1922 à 1965. Dans un secteur réglementé, le rendement juste et équitable est déterminé par l'organisme de réglementation compétent et non par le marché spéculatif et aléatoire de l'immobilier.

112 Je ne crois pas que l'allégation d'effet « confiscatoire » apporte quoi que ce soit au débat juridique. La loi interdit à ATCO de se départir de ses biens sans l'autorisation de la Commission et investit cette dernière du pouvoir d'assortir son autorisation de conditions. Ce n'est donc pas l'*existence* de la compétence qui est en litige, mais plutôt la manière dont la Commission l'a *exercée* en imposant des conditions et, plus particulièrement, en répartissant le profit net tiré de la vente.

E. *La Commission a-t-elle exercé sa compétence irrégulièrement en imposant les conditions qu'elle jugeait « nécessaires dans l'intérêt public »?*

113 Il y a évidemment de nombreuses façons de concevoir « l'intérêt public ». Celle de la Commission tient essentiellement (et de manière inhérente) à son opinion et à son pouvoir discrétionnaire. Même si le cadre législatif de la réglementation des services publics varie d'un ressort à l'autre et qu'aux États-Unis, la pratique doit être interprétée à la lumière de la protection constitutionnelle du droit de propriété, la Commission s'est vu conférer par le législateur albertain un pouvoir plus étendu que celui accordé à la plupart des organismes apparentés. ATCO reconnaît que sa prétention fondée sur le « droit de propriété » ne saurait tenir face à l'intention contraire du législateur, mais elle affirme qu'une telle intention ne ressort pas des lois.

114 La plupart des organismes de réglementation, sinon tous, sont appelés à décider de l'attribution du profit tiré d'un bien dont le coût historique est inclus dans la base tarifaire, mais qui n'est plus nécessaire pour fournir le service. Lorsqu'elle formule ses politiques, la Commission peut tenir compte (et elle tient compte) d'une foule de précédents provenant de nombreux ressorts. Trouver le bon

and investors is a common preoccupation of comparable boards and agencies:

> First, it prevents the utility from degrading the quality, or reducing the quantity, of the regulated service so as to harm consumers. Second, it ensures that the utility maximizes the aggregate economic benefits of its operations, and not merely the benefits flowing to some interest group or stakeholder. Third, it specifically seeks to prevent favoritism toward investors to the detriment of ratepayers affected by the transaction.

(P. W. MacAvoy and J. G. Sidak, "The Efficient Allocation of Proceeds from a Utility's Sale of Assets" (2001), 22 *Energy L.J.* 233, at p. 234)

115 The concern with which Canadian regulators view utilities under their jurisdiction that are speculating in land is not new. In *Re Consumers' Gas Co.*, E.B.R.O. 341-I, June 30, 1976, the Ontario Energy Board considered how to deal with a real estate profit on land which was disposed of at an after-tax profit of over $2 million. The Board stated:

> The Station "B" property was not purchased by Consumers' for land speculation but was acquired for utility purposes. This investment, while non-depreciable, was subject to interest charges and risk paid for through revenues and, until the gas manufacturing plant became obsolete, disposal of the land was not a feasible option. If, in such circumstances, the Board were to permit real estate profit to accrue to the shareholders only, it would tend to encourage real estate speculation with utility capital. In the Board's opinion, the shareholders and the ratepayers should share the benefits of such capital gains. [Emphasis added; para. 326.]

116 Some U.S. regulators also consider it good regulatory policy to allocate part or all of the profit to offset costs in the rate base. In *Re Boston Gas Co.*, 49 P.U.R. 4th 1 (Mass. D.P.U. 1982), the regulator allocated a gain on the sale of land to ratepayers, stating:

compromis dans la répartition du profit entre les clients et les investisseurs est une préoccupation commune aux organismes apparentés à la Commission :

> [TRADUCTION] D'abord, cela permet d'éviter que l'entreprise de services publics ne diminue qualitativement ou quantitativement le service réglementé et ne cause de la sorte un préjudice aux clients. Deuxièmement, elle garantit que l'entreprise maximisera l'ensemble des avantages financiers tirés de ses activités, et non seulement ceux destinés à certains groupes d'intérêt ou à d'autres intéressés. Troisièmement, elle vise précisément à ce que les investisseurs ne soient pas favorisés au détriment des clients touchés par l'opération.

(P. W. MacAvoy et J. G. Sidak, « The Efficient Allocation of Proceeds from a Utility's Sale of Assets » (2001), 22 *Energy L.J.* 233, p. 234)

Ce n'est pas d'hier que les organismes de réglementation canadiens examinent de près les opérations de spéculation foncière auxquelles se livrent les services publics qui leur sont assujettis. Dans la décision *Re Consumers' Gas Co.*, E.B.R.O. 341-I, 30 juin 1976, la Commission de l'énergie de l'Ontario s'est demandé comment devait être considéré le profit de 2 millions de dollars, après impôt, tiré de la vente d'un terrain par une entreprise de services publics. Elle a dit :

> [TRADUCTION] Consumers' n'a pas acquis le bien-fonds (Station B) à des fins de spéculation, mais bien pour les besoins d'un service public. Même si cet investissement n'était pas amortissable, des intérêts et un risque lié à leur taux devaient être absorbés par les revenus et, jusqu'à ce que l'usine de production de gaz ne devienne obsolescente, l'aliénation du bien-fonds n'était pas possible. Par conséquent, si la commission permettait que seuls les actionnaires bénéficient du profit tiré de la vente d'un terrain, elle encouragerait la spéculation sur les biens des services publics. À son avis, ces gains en capital doivent être partagés entre les actionnaires et les clients. [Je souligne; par. 326.]

Certains organismes de réglementation américains jugent également opportun de déduire le profit, en tout ou en partie, de coûts pris en compte dans la base tarifaire. Dans *Re Boston Gas Co.*, 49 P.U.R. 4th 1 (Mass. D.P.U. 1982), l'organisme de réglementation a attribué aux clients le profit tiré de la vente d'un terrain :

The company and its shareholders have received a return on the use of these parcels while they have been included in rate base, and are not entitled to any additional return as a result of their sale. To hold otherwise would be to find that a regulated utility company may speculate in nondepreciable utility property and, despite earning a reasonable rate of return from its customers on that property, may also accumulate a windfall through its sale. We find this to be an uncharacteristic risk/reward situation for a regulated utility to be in with respect to its plant in service. [Emphasis added; p. 26.]

[TRADUCTION] La société et ses actionnaires ont touché un rendement sur l'utilisation de ces parcelles de terrain le temps que leur coût a été inclus dans la base tarifaire, et ils n'ont droit à aucun rendement supplémentaire découlant de leur vente. Conclure le contraire équivaudrait à dire qu'une entreprise de services publics peut tirer avantage d'un bien non amortissable et que même si elle a obtenu de ses clients un rendement raisonnable à l'égard de ce bien, elle peut toucher en sus un profit inattendu en le vendant. Nous estimons que, dans le cas d'une installation en service, il s'agirait d'une situation risques/avantages inhabituelle pour une entreprise réglementée. [Je souligne; p. 26.]

Canadian regulators other than the Board are also concerned with the prospect that decisions of utilities in their regulated business may be skewed under the undue influence of prospective profits on land sales. In *Re Consumers' Gas Co.*, E.B.R.O. 465, March 1, 1991, the Ontario Energy Board determined that a $1.9 million gain on sale of land should be divided equally between shareholders and ratepayers. It held that

117 Au Canada, d'autres organismes de réglementation que la Commission craignent que la perspective de vendre des terrains à profit n'infléchisse les décisions des entreprises de services publics en ce qui concerne leurs activités réglementées. Dans la décision *Re Consumers' Gas Co.*, E.B.R.O. 465, 1er mars 1991, la Commission de l'énergie de l'Ontario a statué que le profit de 1,9 million de dollars réalisé lors de la vente d'un terrain devait être réparti également entre les actionnaires et les clients :

the allocation of 100 percent of the profit from land sales to either the shareholders or the ratepayers might diminish the recognition of the valid concerns of the excluded party. For example, the timing and intensity of land purchase and sales negotiations could be skewed to favour or disregard the ultimate beneficiary. [para. 3.3.8]

[TRADUCTION] . . . attribuer 100 p. 100 du profit tiré de la vente d'un terrain soit aux actionnaires de l'entreprise, soit à ses clients, pourrait diminuer l'attention accordée aux préoccupations légitimes de la partie exclue. Par exemple, le moment de l'acquisition d'un terrain et l'intensité des négociations la précédant pourraient être déterminés de façon à favoriser le bénéficiaire ultime de l'opération, ou à en faire fi. [par. 3.3.8]

The Board's principle of dividing the gain between investors and ratepayers is consistent, as well, with *Re Natural Resource Gas Ltd.*, RP-2002-0147, EB-2002-0446, June 27, 2003, in which the Ontario Energy Board addressed the allocation of a profit on the sale of land and buildings and again stated:

118 Le principe appliqué par la Commission, soit le partage du profit entre les investisseurs et les clients, est également conforme à la décision *Re Natural Resource Gas Ltd.*, RP-2002-0147, EB-2002-0446, 27 juin 2003, dans laquelle la Commission de l'énergie de l'Ontario, après s'être penchée sur la question du profit tiré de la vente d'un terrain et de bâtiments, a de nouveau conclu :

The Board finds that it is reasonable in the circumstances that the capital gains be shared equally between the Company and its customers. In making this finding the Board has considered the non-recurring nature of this transaction. [para. 45]

[TRADUCTION] La Commission juge raisonnable, dans les circonstances, de répartir les gains en capital à parts égales entre l'entreprise et ses clients. Pour arriver à cette conclusion, elle a tenu compte du caractère non récurrent de l'opération. [par. 45]

The wide variety of regulatory treatment of such gains was noted by Kerans J.A. in *TransAlta (1986)*, at pp. 175-76, including *Re Boston Gas Co.*

119 Dans *TransAlta (1986)*, p. 175-176, le juge Kerans a signalé que le sort réservé à de tels gains variait considérablement d'un organisme de

mentioned earlier. In *TransAlta (1986)*, the Board characterized TransAlta's gain on the disposal of land and buildings included in its Edmonton "franchise" as "revenue" within the meaning of the *Hydro and Electric Energy Act*, R.S.A. 1980, c. H-13. (The case therefore did not deal with the power to impose conditions "the Board considers necessary in the public interest".) Kerans J.A. said (at p. 176):

> I do not agree with the Board's decision for reasons later expressed, but it would be fatuous to deny that its interpretation [of the word "revenue"] is one which the word can reasonably bear.

Kerans J.A. went on to find that in that case "[t]he compensation was, for all practical purposes, compensation for loss of franchise" (p. 180) and on that basis the gain in these "unique circumstances" (p. 179) could not, as a matter of law, be characterized as revenue, i.e. applying a correctness standard. The range of regulatory practice on the "gains on sale" issue was similarly noted by Goldie J.A. in *Yukon Energy Corp. v. Utilities Board* (1996), 74 B.C.A.C. 58 (Y.C.A.), at para. 85.

120 A survey of recent regulatory experience in the United States reveals the wide variety of treatment in that country of gains on the sale of undepreciated land. The range includes proponents of ATCO's preferred allocation as well as proponents of the solution adopted by the Board in this case:

> Some jurisdictions have concluded that as a matter of equity, shareholders alone should benefit from any gain realized on appreciated real estate, because ratepayers generally pay only for taxes on the land and do not contribute to the cost of acquiring the property and pay no depreciation expenses. Under this analysis, ratepayers assume no risk for losses and acquire no legal or equitable interest in the property, but rather pay only for the use of the land in utility service.
>
> Other jurisdictions claim that ratepayers should retain some of the benefits associated with the sale of property dedicated to utility service. Those jurisdictions that have adopted an equitable sharing approach agree that a review of regulatory and judicial decisions

réglementation à l'autre, mentionnant à titre d'exemple la décision *Re Boston Gas Co.*, précitée. Dans cette affaire, la Commission avait assimilé à un « revenu » au sens de la *Hydro and Electric Energy Act*, R.S.A. 1980, ch. H-13, le profit réalisé par TransAlta lors de la vente d'un terrain et de bâtiments appartenant à sa « concession » d'Edmonton. (La décision ne portait donc pas sur le pouvoir de la Commission d'imposer les conditions qu'« elle juge nécessaires dans l'intérêt public ».) Le juge Kerans a précisé (p. 176) :

> [TRADUCTION] Pour les motifs exposés ci-après, je ne suis pas d'accord avec la décision de la Commission, mais il serait absurde de ne pas reconnaître que [le mot « revenu »] puisse raisonnablement avoir le sens qu'elle lui prête.

Il a ajouté que [TRADUCTION] « l'indemnisation visait, à toutes fins utiles, à compenser la perte d'une concession » (p. 180), de sorte que, dans « ces circonstances exceptionnelles » (p. 179), le gain ne pouvait en droit être qualifié de revenu suivant la norme de la décision correcte. Dans l'arrêt *Yukon Energy Corp. c. Utilities Board* (1996), 74 B.C.A.C. 58 (C.A.Y.), par. 85, le juge Goldie a lui aussi relevé la diversité de la pratique réglementaire à l'égard du « gain tiré d'une vente ».

Les décisions récentes d'organismes de réglementation des États-Unis révèlent que le sort réservé au gain réalisé lors de la vente d'un terrain non amorti y est aussi très variable et comprend tant la solution préconisée par ATCO que celle retenue par la Commission :

> [TRADUCTION] Certains ressorts ont conclu que, sur le plan de l'équité, seuls les actionnaires doivent bénéficier du gain tiré d'un terrain qui s'est apprécié, car en général, les clients des entreprises de services publics paient les taxes foncières et non le coût d'acquisition et les charges d'amortissement. Suivant ce raisonnement, les clients n'assument aucun risque de perte et n'acquièrent aucun droit sur le bien, y compris en equity.
>
> D'autres estiment que les clients ont droit à une partie des profits résultant de la vente d'un terrain affecté à un service public. Les ressorts qui ont opté pour une répartition équitable conviennent que l'examen des décisions des organismes de réglementation et des cours de

on the issue does not reveal any general principle that requires the allocation of benefits solely to shareholders; rather, the cases show only a general prohibition against sharing benefits on the sale property that has never been reflected in utility rates.

(P. S. Cross, "Rate Treatment of Gain on Sale of Land: Ratepayer Indifference, A New Standard?" (1990), 126 *Pub. Util. Fort.* 44, at p. 44)

Regulatory opinion in the United States favourable to the solution adopted here by the Board is illustrated by *Re Arizona Public Service Co.*, 91 P.U.R. 4th 337 (Ariz. C.C. 1988), at p. 361:

To the extent any general principles can be gleaned from the decisions in other jurisdictions they are: (1) the utility's stockholders are not *automatically* entitled to the gains from all sales of utility property; and (2) ratepayers are not entitled to all or any part of a gain from the sale of property which has never been reflected in the utility's rates. [Emphasis in original.]

Assets purchased with capital reflected in the rate base come and go, but the utility itself endures. What was done by the Board in this case is quite consistent with the "enduring enterprise" theory espoused, for example, in *Re Southern California Water Co.*, 43 C.P.U.C. 2d 596 (1992). In that case, Southern California Water had asked for approval to sell an old headquarters building and the issue was how to allocate its profits on the sale. The Commission held:

Working from the principle of the "enduring enterprise", the gain-on-sale from this transaction should remain within the utility's operations rather than being distributed in the short run directly to either ratepayers or shareholders.

The "enduring enterprise" principle, is neither novel nor radical. It was clearly articulated by the Commission in its seminal 1989 policy decision on the issue of gain-on-sale, D.89-07-016, 32 Cal. P.U.C.2d 233 (*Redding*). Simply stated, to the extent that a utility realizes a gain-on-sale from the liquidation of an asset and replaces it with another asset or obligation while at

justice sur la question ne permet pas de dégager l'exigence générale que le profit soit attribué aux seuls actionnaires, mais seulement une interdiction générale de le répartir lorsque le coût du terrain n'a jamais été inclus dans la base tarifaire.

(P. S. Cross, « Rate Treatment of Gain on Sale of Land : Ratepayer Indifference, A New Standard? » (1990), 126 *Pub. Util. Fort.* 44, p. 44)

La décision *Re Arizona Public Service Co.*, 91 P.U.R. 4th 337 (Ariz. C.C. 1988), illustre le point de vue américain favorable à la solution retenue par la Commission dans la présente affaire (p. 361) :

[TRADUCTION] Les principes généraux qui peuvent être dégagés des décisions rendues dans d'autres ressorts, s'il en est, sont les suivants : (1) les actionnaires d'une entreprise de services publics n'ont pas *automatiquement* droit au gain réalisé lors de toute vente d'un bien affecté au service public; (2) les clients n'ont pas droit à la totalité ou à une partie du profit tiré lors de la vente d'un bien qui n'a jamais été pris en compte pour l'établissement des tarifs. [En italique dans l'original.]

121

La composition de l'actif dont le coût est pris en compte dans la base tarifaire varie au gré des acquisitions et des aliénations, mais l'entreprise, elle, demeure. La démarche de la Commission en l'espèce est tout à fait compatible avec le principe de la « pérennité de l'entreprise » appliqué notamment dans *Re Southern California Water Co.*, 43 C.P.U.C. 2d 596 (1992). Dans cette affaire, Southern California Water avait sollicité l'autorisation de vendre un vieil établissement, et la commission devait décider de l'attribution du profit tiré de l'opération. La commission a conclu :

[TRADUCTION] Partant du principe de la « pérennité de l'entreprise », le profit tiré de l'opération doit être affecté à l'exploitation du service public, et non attribué à court terme aux actionnaires ou aux clients directement.

Ce principe n'est ni nouveau ni absolu. Il a clairement été énoncé dans la décision de principe que la commission a rendue en 1989 concernant le gain réalisé lors d'une vente (D.89-07-016, 32 Cal. P.U.C.2d 233 (*Redding*)). En termes simples, lorsqu'une entreprise de services publics réalise un profit en vendant un bien qu'elle remplace par un autre ou par un titre de créance,

the same time its responsibility to serve its customers is neither relieved nor reduced, then any gain-on-sale should remain within the utility's operation. [p. 604]

122 In my view, neither the Alberta statutes nor regulatory practice in Alberta and elsewhere dictates the answer to the problems confronting the Board. It would have been open to the Board to allow ATCO's application for the entire profit. But the solution it adopted was quite within its statutory authority and does not call for judicial intervention.

F. *ATCO's Arguments*

123 Most of ATCO's principal submissions have already been touched on but I will repeat them here for convenience. ATCO does not really dispute the Board's ability to impose conditions on the sale of land. Rather, ATCO says that what the Board did here violates a number of basic legal protections and principles. It asks the Court to clip the Board's wings.

124 Firstly, ATCO says that customers do not acquire any proprietary right in the company's assets. ATCO, rather than its customers, originally purchased the property, held title to it, and therefore was entitled to any gain on its sale. An allocation of profit to the customers would amount to a confiscation of the corporation's property.

125 Secondly, ATCO says its retention of 100 percent of the gain has nothing to do with the so-called "regulatory compact". The gas customers paid what the Board regarded over the years as a fair price for safe and reliable service. That is what the ratepayers got and that is all they were entitled to. The Board's allocation of part of the profit to the ratepayers amounts to impermissible "retroactive" rate setting.

126 Thirdly, utilities are not entitled to include in the rate base an amount for *depreciation* on land and ratepayers have therefore not repaid ATCO any part of ATCO's original cost, let alone the present value. The treatment accorded gain on sales of depreciated property therefore does not apply.

sans que son obligation de servir la clientèle ne soit supprimée ou réduite, le profit doit être affecté à l'exploitation de l'entreprise. [p. 604]

À mon avis, ni les lois de l'Alberta ni la pratique réglementaire dans cette province et dans d'autres ressorts ne commandaient une décision en particulier. La Commission aurait pu accueillir la demande d'ATCO et lui attribuer la totalité du profit. Mais la solution qu'elle a retenue n'outrepassait aucunement sa compétence légale et ne justifie pas une intervention judiciaire.

F. *L'argumentation d'ATCO*

Les principaux arguments d'ATCO ont pour la plupart été abordés, mais, par souci de clarté, je les rappellerai. ATCO ne conteste pas vraiment le pouvoir de la Commission d'assortir de conditions la vente d'un terrain. Elle soutient plutôt que la Commission a violé en l'espèce un certain nombre de garanties et nous demande de restreindre sa marge de manœuvre.

Premièrement, ATCO prétend que les clients n'acquièrent aucun droit de propriété sur les biens de l'entreprise. C'est elle, et non ses clients, qui a initialement acheté le bien en question et qui en est devenue propriétaire, ce qui lui donnait droit à tout profit tiré de sa vente. Selon elle, attribuer le profit aux clients équivaut à confisquer l'actif de l'entreprise.

Deuxièmement, ATCO prétend que son droit à la totalité du profit n'a rien à voir avec le « pacte réglementaire ». Ses clients ont payé un prix que, d'une année à l'autre, la Commission a jugé raisonnable en contrepartie d'un service sûr et fiable. C'est ce qu'ils ont obtenu et c'est tout ce à quoi ils avaient droit. En leur attribuant une partie du profit, la Commission s'est indûment livrée à une tarification « rétroactive ».

Troisièmement, une entreprise de services publics ne peut *amortir* un terrain dans sa base tarifaire, de sorte que les clients n'ont pas défrayé ATCO de quelque partie du coût historique du terrain en question, encore moins en fonction de sa valeur actuelle. Le traitement réservé au profit tiré de la vente d'un bien amorti ne s'applique donc pas.

Fourthly, ATCO complains that the Board's solution is asymmetrical. Ratepayers are given part of the benefit of an increase in land values without, in a falling market, bearing any part of the burden of losses on the disposition of land.

127 Quatrièmement, ATCO reproche à la solution de la Commission de créer une disparité. Les clients se voient attribuer une partie du profit résultant de l'appréciation d'un terrain sans pour autant être tenus, advenant une contraction du marché, d'assumer une partie des pertes subies lors de son aliénation.

In my view, these are all arguments that should be (and were) properly directed to the Board. There are indeed precedents in the regulatory field for what ATCO proposes, just as there are precedents for what the ratepayers proposed. It was for the Board to decide what conditions in these particular circumstances were necessary in the public interest. The Board's solution in this case is well within the range of reasonable options, as I will endeavour to demonstrate.

128 À mon avis, ce sont toutes des prétentions qui devaient être dûment formulées devant la Commission (et qui l'ont été). Certaines décisions d'organismes de réglementation étayent la thèse d'ATCO, d'autres appuient celle de ses clients. Il appartenait à la Commission de décider, au vu des circonstances, quelles conditions étaient nécessaires dans l'intérêt public. Comme je vais m'efforcer de le démontrer, la solution adoptée par la Commission en l'espèce s'inscrivait parmi celles pour lesquelles elle pouvait raisonnablement opter.

1. The Confiscation Issue

In its factum, ATCO says that "[t]he property belonged to the owner of the utility and the Board's proposed distribution cannot be characterized otherwise than as being confiscatory" (respondent's factum, at para. 6). ATCO's argument overlooks the obvious difference between investment in an unregulated business and investment in a regulated utility where the regulator sets the return on investment, not the marketplace. In *Re Southern California Gas Co.*, 118 P.U.R. 4th 81 (C.P.U.C. 1990) ("*SoCalGas*"), the regulator pointed out:

1. La question de l'effet confiscatoire

129 Dans son mémoire, ATCO affirme que [TRADUCTION] « [l]es biens appartenaient au propriétaire du service public et que la répartition projetée par la Commission ne peut avoir qu'un effet confiscatoire » (mémoire de l'intimée, par. 6). Cet argument ne tient pas compte de la différence manifeste entre un investissement dans une entreprise non réglementée et un investissement dans un service public réglementé, le taux de rendement étant, dans ce dernier cas, fixé par un organisme de réglementation, et non par le marché. Dans la décision *Re Southern California Gas Co.*, 118 P.U.R. 4th 81 (C.P.U.C. 1990) (« *SoCalGas* »), l'organisme de réglementation a fait remarquer :

In the non-utility private sector, investors are not guaranteed to earn a fair return on such sunk investment. Although shareholders and bondholders provide the initial capital investment, the ratepayers pay the taxes, maintenance, and other costs of carrying utility property in rate base over the years, and thus insulate utility investors from the risk of having to pay those costs. Ratepayers also pay the utility a fair return on property (including land) while it is in rate base, compensate the utility for the diminishment of the value of its depreciable property over time through depreciation

[TRADUCTION] Dans le secteur privé, qui exclut donc les services publics, l'investisseur n'est pas assuré d'un rendement raisonnable sur un tel investissement irrécupérable. Bien que les actionnaires et les détenteurs d'obligations fournissent le capital initial, les clients paient au fil des ans, par le truchement de la base tarifaire, les taxes, les frais d'entretien et les autres coûts liés à la possession du bien, de sorte que la personne qui investit dans un service public ne risque pas d'avoir à supporter ces coûts. Les clients paient également un rendement raisonnable pendant que le bien (terrain

accounting, and bear the risk that they must pay depreciation and a return on prematurely retired rate base property. [p. 103]

(It is understood, of course, that the Board does not appropriate the actual proceeds of sale. What happens is that an amount *equivalent* to two-thirds of the profit is included in the calculation of ATCO's current cost base for rate-making purposes. In that way, there is a notional distribution of the benefit of the gain amongst the competing stakeholders.)

130 ATCO's argument is frequently asserted in the United States under the flag of constitutional protection for "property". Constitutional protection has not however prevented allocation of all or part of such gains to the U.S. ratepayers. One of the leading U.S. authorities is *Democratic Central Committee of the District of Columbia v. Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (D.C. Cir. 1973). In that case, the assets at issue were parcels of real estate which had been employed in mass transit operations but which were no longer needed when the transit system converted to buses. The regulator awarded the profit on the appreciated land values to the shareholders but the Court of Appeals reversed the decision, using language directly applicable to ATCO's "confiscation" argument:

We perceive no impediment, constitutional or otherwise, to recognition of a ratemaking principle enabling ratepayers to benefit from appreciations in value of utility properties accruing while in service. We believe the doctrinal consideration upon which pronouncements to the contrary have primarily rested has lost all present-day vitality. Underlying these pronouncements is a basic legal and economic thesis — sometimes articulated, sometimes implicit — that utility assets, though dedicated to the public service, remain exclusively the property of the utility's investors, and that growth in value is an inseparable and inviolate incident of that property interest. The precept of private ownership historically pervading our jurisprudence led naturally to such a thesis, and early decisions in the ratemaking field lent some support to it; if still viable, it strengthens the investor's claim. We think, however, after careful

compris) est inclus dans la base tarifaire, ils indemnisent l'entreprise de la dépréciation d'un bien amortissable selon la méthode de la prise en charge par amortissement et ils courent le risque de payer l'amortissement et un rendement pour un bien inclus dans la base tarifaire qui est mis hors service prématurément. [p. 103]

(La Commission ne fait évidemment pas main basse sur le produit de la vente. Pour les besoins de la tarification, un montant *équivalant* aux deux tiers du profit est en fait pris en compte pour établir la base tarifaire actuelle d'ATCO. Le profit est donc réparti de manière abstraite entre les intéressés concurrents.)

L'argument d'ATCO est fréquemment invoqué aux États-Unis sur le fondement de la protection constitutionnelle du « droit de propriété », laquelle n'a toutefois pas empêché que tout ou partie du profit en cause soit attribué aux clients de services publics américains. L'un des arrêts de principe aux États-Unis est *Democratic Central Committee of the District of Columbia c. Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (D.C. Cir. 1973). Dans cette affaire, des parcelles de terrain affectées au transport en commun étaient devenues superflues lorsque l'entreprise avait remplacé ses trolleybus par des autobus. L'organisme de réglementation a attribué aux actionnaires le profit tiré de la vente des terrains dont la valeur s'était appréciée, mais la cour d'appel a infirmé la décision en tenant un raisonnement directement applicable à l'effet « confiscatoire » allégué par ATCO :

[TRADUCTION] Nous ne voyons aucun obstacle, constitutionnel ou autre, à la reconnaissance d'un principe de tarification permettant aux clients de bénéficier de l'appréciation d'un bien survenue pendant son affectation au service public. Nous croyons que la doctrine fondant essentiellement les décisions contraires n'est plus pertinente. Un principe juridique et économique fondamental — parfois formulé en termes exprès, parfois implicite —, sous-tend ces décisions, savoir qu'un bien affecté à un service public demeure la propriété des seuls investisseurs de l'entreprise et que son appréciation est un élément indissociable et inviolable de ce droit de propriété. La notion de propriété privée qui imprègne notre jurisprudence a naturellement mené à l'application de ce principe, lequel a obtenu un certain appui dans les premières décisions en matière de tarification. S'il est encore valable, ce principe étaye la

exploration, that the foundations for that approach, and the conclusion it seemed to indicate, have long since eroded away. [p. 800]

The court's reference to "pronouncements" which have "lost all present-day vitality" likely includes *Board of Public Utility Commissioners v. New York Telephone Co.*, 271 U.S. 23 (1976), a decision relied upon in this case by ATCO. In that case, the Supreme Court of the United States said:

> Customers pay for service, not for the property used to render it. Their payments are not contributions to depreciation or other operating expenses or to capital of the company. By paying bills for service they do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company. Property paid for out of moneys received for service belongs to the company just as does that purchased out of proceeds of its bonds and stock. [p. 32]

In that case, the regulator belatedly concluded that the level of depreciation allowed the New York Telephone Company had been excessive in past years and sought to remedy the situation in the current year by retroactively adjusting the cost base. The court held that the regulator had no power to re-open past rates. The financial fruits of the regulator's errors in past years now belonged to the company. That is not this case. No one contends that the Board's prior rates, based on ATCO's original investment, were wrong. In 2001, when the matter came before the Board, the Board had jurisdiction to approve or not approve the proposed sale. It was not a done deal. The receipt of any profit by ATCO was prospective only. As explained in *Re Arizona Public Service Co.*:

> In *New York Telephone*, the issue presented was whether a state regulatory commission could use excessive depreciation accruals from prior years to reduce rates for future service and thereby set rates which did not yield a just return. . . . [T]he Court simply reiterated and provided the reasons for a ratemaking truism: rates must be designed to produce enough revenue to pay

prétention de l'investisseur. Après mûre réflexion, nous pensons que ses fondements se sont depuis longtemps effrités et que la conclusion qu'il semblait dicter ne vaut plus. [p. 800]

Ces « décisions » qui ne sont « plus pertinente[s] » englobent sans doute *Board of Public Utility Commissioners c. New York Telephone Co.*, 271 U.S. 23 (1976), une décision invoquée par ATCO en l'espèce et dans laquelle la Cour suprême des États-Unis a dit :

> [TRADUCTION] Les clients paient un service, et non le bien servant à sa prestation. Leurs paiements ne sont pas affectés à l'amortissement ou aux autres frais d'exploitation, non plus qu'au capital de l'entreprise. En acquittant leurs factures, les clients n'acquièrent aucun droit, suivant la loi ou l'equity, sur les biens utilisés pour fournir le service ou sur les fonds de l'entreprise. Les biens acquis avec les sommes reçues en contrepartie des services appartiennent à l'entreprise, tout comme ceux achetés avec les fonds obtenus par l'émission d'actions et d'obligations. [p. 32]

Dans cette affaire, ayant conclu tardivement que l'amortissement autorisé pour New York Telephone Company les années précédentes était trop élevé, l'organisme de réglementation avait tenté de corriger la situation pendant l'exercice en cours en rajustant rétroactivement la base tarifaire. La cour a statué que l'organisme n'avait pas le pouvoir de réviser une tarification antérieure. Les avantages financiers découlant des erreurs commises par l'organisme étaient désormais acquis à l'entreprise. Le contexte n'est pas le même en l'espèce. Nul ne prétend que la tarification antérieure établie par la Commission en fonction du coût historique était erronée. En 2001, lorsqu'elle a été saisie de l'affaire, la Commission avait le pouvoir d'autoriser ou non la vente projetée. L'opération n'avait pas encore été conclue. La réalisation d'un profit par ATCO n'était qu'une possibilité. Comme on l'a expliqué dans *Re Arizona Public Service Co.* :

> [TRADUCTION] Dans *New York Telephone*, le tribunal devait déterminer si l'organisme de réglementation de l'État en question pouvait affecter à la réduction des tarifs l'excédent accumulé aux fins d'amortissement les années précédentes et ainsi fixer des tarifs qui ne produisaient pas un rendement raisonnable. [. . .] [L]a Cour a simplement repris un truisme en l'expliquant : les

current (reasonable) operating expenses and provide a fair return to the utility's investors. If it turns out that, for whatever reason, existing rates have produced too much or too little income, the past is past. Rates are raised or lowered to reflect current conditions; they are not designed to pay back past excessive profits or recoup past operating losses. In contrast, the issue in this proceeding is whether for ratemaking purposes a utility's test year income from sales of utility service can include its income from sales of utility property. The United States Supreme Court's decision in *New York Telephone* does not address that issue. [Emphasis added; p. 361.]

tarifs doivent être établis de façon que les revenus permettent d'acquitter les charges (raisonnables) d'exploitation courantes et que les investisseurs de l'entreprise obtiennent un rendement raisonnable. Lorsque, pour une raison ou une autre, les tarifs fixés produisent trop de revenus ou pas assez, on ne peut revenir en arrière. On augmente les tarifs ou on les réduit pour tenir compte de la situation actuelle; leur fixation ne vise pas la restitution de profits excessifs antérieurs ou la compensation de pertes d'exploitation antérieures. En l'espèce, il s'agit plutôt de déterminer si, pour l'établissement des tarifs, le revenu provenant de la fourniture d'un service public pendant une année de référence peut comprendre le produit de la vente de biens de l'entreprise de services publics. La décision *New York Telephone* de la Cour suprême des États-Unis ne porte pas sur cette question. [Je souligne; p. 361.]

131 More recently, the allocation of gain on sale was addressed by the California Public Utilities Commission in *SoCalGas*. In that case, as here, the utility (SoCalGas) wished to sell land and buildings located (in that case) in downtown Los Angeles. The Commission apportioned the gain on sale between the shareholders and the ratepayers, concluding that:

Plus récemment, dans la décision *SoCalGas*, la commission californienne de surveillance des services publics s'est penchée sur la question de l'attribution du profit tiré d'une aliénation. Comme dans la présente affaire, l'entreprise de services publics (SoCalGas) souhaitait vendre un terrain et des bâtiments situés (dans ce cas) au centre-ville de Los Angeles. La commission a réparti le profit entre les actionnaires et les clients de l'entreprise et a conclu :

> We believe that the issue of who owns the utility property providing utility service has become a red herring in this case, and that ownership alone does not determine who is entitled to the gain on the sale of the property providing utility service when it is removed from rate base and sold. [p. 100]

> [TRADUCTION] Nous croyons que la question de savoir à qui appartient le bien affecté au service public est devenue un faux problème en l'espèce et que la propriété ne permet pas à elle seule de déterminer qui a droit au profit lorsque ce bien cesse d'être inclus dans la base tarifaire et est vendu. [p. 100]

132 ATCO argues in its factum that ratepayers "do not acquire any interest, legal or equitable, in the property used to provide the service or in the funds of the owner of the utility" (para. 2). In *SoCalGas*, the regulator disposed of this point as follows:

ATCO soutient dans son mémoire que les clients [TRADUCTION] « n'acquièrent aucun droit, suivant la loi ou l'equity, sur les biens utilisés pour fournir le service, non plus que sur les fonds de l'entreprise » (par. 2). À cet égard, voici ce qu'a conclu l'organisme de réglementation dans *SoCalGas* :

> No one seriously argues that ratepayers acquire title to the physical property assets used to provide utility service; DRA [Division of Ratepayer Advocates] argues that the gain on sale should reduce future revenue requirements not because ratepayers own the property, but rather because they paid the costs and faced the risks associated with that property while it was in rate base providing public service. [p. 100]

> [TRADUCTION] Personne ne prétend sérieusement que les clients acquièrent un droit de propriété sur les biens affectés au service public; la DRA [Division of Ratepayer Advocates] soutient que le profit tiré de leur vente doit être retranché des besoins en revenus ultérieurs non pas parce que les clients sont propriétaires de ces biens, mais parce qu'ils en ont payé les coûts et assumé les risques pendant leur affectation au service public et leur inclusion dans la base tarifaire. [p. 100]

This "risk" theory applies in Alberta as well. Over the last 80 years, there have been wild swings in Alberta real estate, yet through it all, in bad times and good, the ratepayers have guaranteed ATCO a just and equitable return on its investment in *this* land and *these* buildings.

Cette considération liée aux « risques » vaut également en Alberta. Pendant les 80 dernières années, le marché albertain de l'immobilier a connu des fluctuations considérables, mais durant toute cette période, que la conjoncture ait été favorable ou non, les clients ont garanti à ATCO un rendement juste et équitable pour le terrain et les bâtiments *considérés en l'espèce*.

The notion that the division of risk justifies a division of the net gain was also adopted by the regulator in *SoCalGas*:

133 L'approche suivant laquelle le partage des risques emporte le partage du gain net a également été retenue dans *SoCalGas* :

> Although the shareholders and bondholders provided the initial capital investment, the ratepayers paid the taxes, maintenance, and other costs of carrying the land and buildings in rate base over the years, and paid the utility a fair return on its unamortized investment in the land and buildings while they were in rate base. [p. 110]

> [TRADUCTION] Même si les actionnaires et les détenteurs d'obligations ont fourni le capital initial, les clients ont payé au fil des ans, par le truchement de la base tarifaire, les taxes, les frais d'entretien et les autres coûts liés à la possession du terrain et des bâtiments et ils ont assuré à l'entreprise un rendement raisonnable selon la valeur non amortie du terrain et des bâtiments pendant la période où leur coût a été inclus dans la base tarifaire. [p. 110]

In other words, even in the United States, where property rights are constitutionally protected, ATCO's "confiscation" point is rejected as an oversimplification.

Autrement dit, même aux États-Unis où le droit de propriété est protégé par la Constitution, la thèse de l'effet « confiscatoire » avancée par ATCO est rejetée au motif qu'elle est simpliste.

My point is not that the Board's allocation in this case is necessarily correct in all circumstances. Other regulators have determined that the public interest requires a different allocation. The Board proceeds on a "case-by-case" basis. My point simply is that the Board's response in this case cannot be considered "confiscatory" in any proper use of the term, and is well within the range of what are regarded in comparable jurisdictions as appropriate regulatory responses to the allocation of the gain on sale of land whose original investment has been included by the utility itself in its rate base. The Board's decision is protected by a deferential standard of review and in my view it should not have been set aside.

134 Je ne prétends pas que l'attribution du profit en l'espèce convient nécessairement en toute circonstance. D'autres organismes de réglementation ont jugé que l'intérêt public commande une attribution différente. La Commission tranche au cas par cas. Je dis simplement que la mesure retenue ne peut être qualifiée de « confiscatoire » dans quelque acception de ce terme et qu'elle fait partie des solutions jugées acceptables dans des ressorts comparables en ce qui concerne l'attribution du profit tiré de la vente d'un terrain dont l'entreprise de services publics a elle-même inclus le coût historique dans sa base tarifaire. La déférence s'impose en l'espèce et, à mon avis, la décision de la Commission n'aurait pas dû être annulée.

2. The Regulatory Compact

2. Le pacte réglementaire

The Board referred in its decision to the "regulatory compact" which is a loose expression suggesting that in exchange for a statutory monopoly

135 Dans sa décision, la Commission renvoie au « pacte réglementaire », notion aux contours flous selon laquelle, en contrepartie d'un monopole

and receipt of revenue on a cost plus basis, the utility accepts limitations on its rate of return and its freedom to do as it wishes with property whose cost is reflected in its rate base. This was expressed in the *Washington Metropolitan Area Transit* case by the U.S. Court of Appeals for the District of Columbia Circuit as follows:

> The ratemaking process involves fundamentally "a balancing of the investor and the consumer interests". The investor's interest lies in the integrity of his investment and a fair opportunity for a reasonable return thereon. The consumer's interest lies in governmental protection against unreasonable charges for the monopolistic service to which he subscribes. In terms of property value appreciations, the balance is best struck at the point at which the interests of both groups receive maximum accommodation. [p. 806]

136 ATCO considers that the Board's allocation of profit violated the regulatory compact not only because it is confiscatory but because it amounts to "retroactive rate making". In *Northwestern Utilities Ltd. v. City of Edmonton*, [1979] 1 S.C.R. 684, Estey J. stated, at p. 691:

> It is clear from many provisions of *The Gas Utilities Act* that the Board must act prospectively and may not award rates which will recover expenses incurred in the past and not recovered under rates established for past periods.

137 As stated earlier, the Board in this case was addressing a prospective receipt and allocated two thirds of it to a prospective (not retroactive) ratemaking exercise. This is consistent with regulatory practice, as is illustrated by *New York Water Service Corp. v. Public Service Commission*, 208 N.Y.S.2d 857 (1960). In that case, a utility commission ruled that gains on the sale of real estate should be taken into account to reduce rates annually over the following period of 17 years :

> If land is sold at a profit, it is required that the profit be added to, i.e., "credited to", the depreciation reserve, so

conféré par la loi et d'un revenu calculé suivant la méthode du coût d'achat majoré, l'entreprise de services publics accepte de voir son rendement limité de même que sa liberté de se départir des biens dont le coût est pris en compte pour établir sa base tarifaire. C'est ce qui ressort de l'arrêt *Washington Metropolitan Area Transit* de la Cour d'appel des États-Unis (circuit du district de Columbia) :

> [TRADUCTION] Le processus de tarification consiste essentiellement à « mettre en balance l'intérêt de l'investisseur et celui du consommateur ». L'intérêt de l'investisseur est de protéger son investissement et d'avoir une possibilité raisonnable de toucher un rendement acceptable. L'intérêt du consommateur réside dans la protection gouvernementale contre la tarification déraisonnable de services fournis dans un contexte monopolistique. Pour ce qui est de l'appréciation d'un bien, l'équilibre optimal est atteint lorsque les intérêts de l'un et de l'autre sont respectés le plus possible. [p. 806]

ATCO estime que la manière dont la Commission a attribué le profit contrevient au pacte réglementaire non seulement en raison de son effet confiscatoire, mais aussi parce qu'il s'agit d'une « tarification rétroactive ». Dans l'arrêt *Northwestern Utilities Ltd. c. Ville d'Edmonton*, [1979] 1 R.C.S. 684, le juge Estey a dit ce qui suit à la p. 691 :

> Il ressort clairement de plusieurs dispositions de *The Gas Utilities Act* que la Commission n'agit que pour l'avenir et ne peut fixer des tarifs qui permettraient à l'entreprise de recouvrer des dépenses engagées antérieurement et que les tarifs précédents n'avaient pas suffi à compenser.

Je le répète, la Commission était appelée à se prononcer sur une rentrée projetée et elle a décidé que les deux tiers devraient être pris en compte dans la tarification ultérieure (et non antérieure), ce qui est conforme à la pratique réglementaire. Par exemple, dans la décision *New York Water Service Corp. c. Public Service Commission*, 208 N.Y.S.2d 857 (1960), l'organisme de réglementation a statué que le profit réalisé lors de la vente d'un terrain devrait servir à réduire les tarifs pour les 17 années suivantes :

> [TRADUCTION] Lorsqu'un terrain est vendu à profit, le gain doit être ajouté à l'amortissement cumulé, c.-à-d.

that there is a corresponding reduction of the rate base and resulting return. [p. 864]

The regulator's order was upheld by the New York State Supreme Court (Appellate Division).

More recently, in *Re Compliance with the Energy Policy Act of 1992*, 62 C.P.U.C. 2d 517 (1995), the regulator commented:

> . . . we found it appropriate to allocate the principal amount of the gain to offset future costs of headquarters facilities, because ratepayers had borne the burden of risks and expenses while the property was in rate-base. At the same time, we found that it was equitable to allocate a portion of the benefits from the gain-on-sale to shareholders in order to provide a reasonable incentive to the utility to maximize the proceeds from selling such property and compensate shareholders for any risks borne in connection with holding the former property. [p. 529]

The emphasis in all these cases is on balancing the interests of the shareholders and the ratepayers. This is perfectly consistent with the "regulatory compact" approach reflected in the Board doing what it did in this case.

3. Land as a Non-Depreciable Asset

The Alberta Court of Appeal drew a distinction between gains on sale of land, whose original cost is not depreciated (and thus is not repaid in increments through the rate base) and depreciated property such as buildings where the rate base does include a measure of capital repayment and which in that sense the ratepayers have "paid for". The Alberta Court of Appeal held that the Board was correct to credit the rate base with an amount equivalent to the depreciation paid in respect of the buildings (this is the subject matter of ATCO's cross-appeal). Thus, in this case, the land was still carried on ATCO's books at its original price of $83,720 whereas the original $596,591 cost of the buildings had been depreciated through the rates charged customers to a net book value of $141,525.

« porté à son crédit », de manière à réduire proportionnellement la base tarifaire et, par conséquent, le rendement. [p. 864]

L'ordonnance a été confirmée par la Cour suprême de l'État de New York (section d'appel).

138 Plus récemment, dans la décision *Re Compliance with the Energy Policy Act of 1992*, 62 C.P.U.C. 2d 517 (1995), l'organisme de réglementation a dit :

> [TRADUCTION] . . . nous avons jugé approprié de déduire la plus grande partie du profit des coûts futurs liés au siège de l'entreprise parce que les clients avaient assumé les risques et les charges pendant l'inclusion du bien dans la base tarifaire. Nous avons également jugé équitable d'attribuer une partie du profit aux actionnaires afin d'inciter raisonnablement l'entreprise à obtenir le meilleur prix de vente possible et d'indemniser les actionnaires des risques inhérents à la possession du bien. [p. 529]

139 Toutes ces décisions mettent l'accent sur la mise en balance des intérêts des actionnaires et des clients, ce qui est tout à fait compatible avec la théorie du « pacte réglementaire » qui sous-tend la décision de la Commission en l'espèce.

3. Le terrain en tant que bien non amortissable

140 La Cour d'appel de l'Alberta a établi une distinction entre le profit tiré de la vente d'un terrain, dont le coût historique n'est pas amorti (et qui n'est donc pas graduellement remboursé par le truchement de la base tarifaire), et le profit tiré de la vente d'un bien amorti, comme un bâtiment, pour lequel la base tarifaire opère un certain remboursement du capital et qui, en ce sens, « a été payé » par les clients. Elle a conclu que la Commission avait eu raison d'inclure dans la base tarifaire l'équivalent de l'amortissement consenti pour les bâtiments (l'objet du pourvoi incident d'ATCO). Ainsi, en l'espèce, alors que la valeur du terrain était encore reportée dans les comptes d'ATCO au coût historique de 83 720 $, les bâtiments, payés initialement 596 591 $, avaient été amortis dans les tarifs exigés des consommateurs et leur valeur comptable nette s'établissait à 141 525 $.

141 Regulatory practice shows that many (not all) regulators also do not accept the distinction (for this purpose) between depreciable and non-depreciable assets. In *Re Boston Gas Co.* for example (cited in *TransAlta (1986)*, at p. 176), the regulator held:

> . . . the company's ratepayers have been paying a return on this land as well as all other costs associated with its use. The fact that land is a nondepreciable asset because its useful value is not ordinarily diminished through use is, we find, irrelevant to the question of who is entitled to the proceeds on the sales of this land. [p. 26]

142 In *SoCalGas*, as well, the Commission declined to make a distinction between the gain on sale of depreciable, as compared to non-depreciable, property, stating: "We see little reason why land sales should be treated differently" (p. 107). The decision continued:

> In short, whether an asset is depreciated for rate-making purposes or not, ratepayers commit to paying a return on its book value for as long as it is used and useful. Depreciation simply recognizes the fact that certain assets are consumed over a period of utility service while others are not. The basic relationship between the utility and its ratepayers is the same for depreciable and non-depreciable assets. [Emphasis added; p. 107.]

143 In *Re California Water Service Co.*, 66 C.P.U.C. 2d 100 (1996), the regulator commented that:

> Our decisions generally find no reason to treat gain on the sale of nondepreciable property, such as bare land, different[ly] than gains on the sale of depreciable rate base assets and land in PHFU [plant held for future use]. [p. 105]

144 Again, my point is not that the regulator *must* reject any distinction between depreciable and non-depreciable property. Simply, my point is that the distinction does not have the controlling weight as contended by ATCO. In Alberta, it is up to the

Il ressort de la pratique réglementaire que de nombreux organismes de réglementation (et non tous) refusent de faire une distinction (à cette fin) entre les biens amortissables et les biens non amortissables. Dans la décision *Re Boston Gas Co.* (citée dans *TransAlta (1986)*, p. 176), par exemple, l'organisme a conclu :

> [TRADUCTION] . . . les clients de l'entreprise ont versé un rendement et payé tous les autres coûts afférents à l'utilisation du terrain. Le fait qu'il s'agit d'un bien non amortissable — son utilisation ne diminuant habituellement pas sa valeur d'usage — n'a rien à voir avec la question de savoir qui a droit au produit de sa vente. [p. 26]

Dans *SoCalGas*, l'organisme de réglementation a également refusé de faire une distinction entre le profit réalisé lors de la vente d'un bien amortissable et celui issu de la vente d'un bien non amortissable, affirmant à la p. 107, qu'[TRADUCTION] « [i]l ne voyait pas pourquoi des ventes de terrains devraient être traitées différemment » et ajoutant :

> [TRADUCTION] En somme, les clients s'engagent à verser un rendement selon la valeur comptable, que le bien soit amorti ou non pour les besoins de la tarification, et ce, tant que le bien est employé et susceptible de l'être. L'amortissement tient simplement compte du fait que certains biens, contrairement à d'autres, se détériorent durant leur affectation au service public. Fondamentalement, la relation entre l'entreprise et ses clients demeure la même qu'il s'agisse de biens amortissables ou non. [Je souligne; p. 107.]

Dans *Re California Water Service Co.*, 66 C.P.U.C. 2d 100 (1996), l'organisme de réglementation a fait la remarque suivante :

> [TRADUCTION] Dans nos décisions, nous concluons généralement qu'il n'y a pas lieu de traiter différemment le profit réalisé lors de la vente d'un bien non amortissable, comme un terrain nu, et celui issu de la vente d'un bien amortissable dont le coût a été inclus dans la base tarifaire ou d'un terrain détenu pour usage ultérieur. [p. 105]

Encore une fois, je ne dis pas que l'organisme de réglementation *doit* systématiquement écarter toute distinction entre un bien amortissable et un bien non amortissable. Je dis simplement que la distinction n'est pas aussi déterminante que le

Board to determine what allocations are necessary in the public interest as conditions of the approval of sale. ATCO's attempt to limit the Board's discretion by reference to various doctrine is not consistent with the broad statutory language used by the Alberta legislature and should be rejected.

prétend ATCO. En Alberta, la Commission peut autoriser une vente à la condition que le produit qui en est tiré soit réparti comme elle le juge nécessaire dans l'intérêt public. La limitation du pouvoir discrétionnaire de la Commission, alléguée par ATCO sur le fondement de différents points de vue doctrinaux, n'est pas compatible avec les termes généraux employés par le législateur albertain et doit être rejetée.

4. Lack of Reciprocity

4. L'absence de réciprocité

145 ATCO argues that the customers should not profit from a rising market because if the land loses value it is ATCO, and not the ratepayers, that will absorb the loss. However, the material put before the Court suggests that the Board takes into account both gains *and* losses. In the following decisions the Board stated, repeated, and repeated again its "general rule" that

ATCO soutient que les clients ne devraient pas tirer avantage d'un marché haussier, car c'est elle, et non eux, qui subirait la perte si la valeur du terrain diminuait. Toutefois, la documentation présentée à notre Cour donne à penser que la Commission tient compte des profits *et* des pertes. Dans les décisions mentionnées ci-après, elle énonce et rappelle, puis rappelle encore, le « principe général » :

the Board considers that any profit or loss (being the difference between the net book value of the assets and the sale price of those assets) resulting from the disposal of utility assets should accrue to the customers of the utility and not to the owner of the utility. [Emphasis added.]

[TRADUCTION] . . . la Commission estime que les profits ou les pertes (soit la différence entre la valeur comptable nette et le produit de la vente) résultant de la vente de biens affectés à un service public doivent être attribués aux clients de l'entreprise de services publics, et non à son propriétaire. [Je souligne.]

(See *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84116, October 12, 1984, at p. 17; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Decision No. E84115, October 12, 1984, at p. 12; *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Decision No. E84113, October 12, 1984, at p. 23.)

(Voir *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision n^{o} E84116, 12 octobre 1984, p. 17; *Re TransAlta Utilities Corp.*, Alta. P.U.B., Décision n^{o} E84115, 12 octobre 1984, p. 12; *Re Canadian Western Natural Gas Co.*, Alta. P.U.B., Décision n^{o} E84113, 12 octobre 1984, p. 23.)

146 In *Re Alberta Government Telephones*, Alta. P.U.B., Decision No. E84081, June 29, 1984, the Board reviewed a number of regulatory approaches (including *Re Boston Gas Co.*, previously mentioned) with respect to gains on sale and concluded with respect to its own practice, at p. 12:

Dans *Re Alberta Government Telephones*, Alta. P.U.B., Décision n^{o} E84081, 29 juin 1984, la Commission a examiné un certain nombre de décisions d'organismes de réglementation (y compris *Re Boston Gas Co.*, précitée) portant sur le profit tiré d'une vente et a dit ce qui suit au sujet de ses propres décisions (p. 12) :

The Board is aware that it has not applied any consistent formula or rule which would automatically determine the accounting procedure to be followed in the treatment of gains or losses on the disposition of utility assets. The reason for this is that the Board's determination of what is fair and reasonable rests on the merits or facts of each case.

[TRADUCTION] La Commission est consciente de n'avoir pas appliqué une formule ou une règle uniforme permettant de déterminer automatiquement la procédure comptable à suivre à l'égard du profit ou de la perte résultant de l'aliénation d'un bien affecté à un service public. Il en est ainsi parce qu'elle décide de ce qui est juste et raisonnable en fonction du fond ou des faits de chaque affaire.

147 ATCO's contention that it alone is burdened with the risk on land that *declines* in value overlooks the fact that in a falling market the utility continues to be entitled to a rate of return on its original investment, even if the market value at the time is substantially less than its original investment. As pointed out in *SoCalGas*:

> If the land actually does depreciate in value below its original cost, then one view could be that the steady rate of return [the ratepayers] have paid for the land over time has actually overcompensated investors. Thus, there is symmetry of risk and reward associated with rate base land just as there is with regard to depreciable rate base property. [p. 107]

II. Conclusion

148 In summary, s. 15(3) of the AEUBA authorized the Board in dealing with ATCO's application to approve the sale of the subject land and buildings to "impose any additional conditions that the Board considers necessary in the public interest". In the exercise of that authority, and having regard to the Board's "general supervision over all gas utilities, and the owners of them" (GUA, s. 22(1)), the Board made an allocation of the net gain for the public policy reasons which it articulated in its decision. Perhaps not every regulator and not every jurisdiction would exercise the power in the same way, but the allocation of the gain on an asset ATCO sought to withdraw from the rate base was a decision the Board was mandated to make. It is not for the Court to substitute its own view of what is "necessary in the public interest".

III. Disposition

149 I would allow the appeal, set aside the decision of the Alberta Court of Appeal, and restore the decision of the Board, with costs to the City of Calgary both in this Court and in the court below. ATCO's cross-appeal should be dismissed with costs.

La prétention selon laquelle ATCO assume seule le risque que la valeur d'un terrain *diminue* ne tient pas compte du fait que s'il y a contraction du marché, l'entreprise de services publics continue de bénéficier d'un rendement fondé sur le coût historique même si la valeur marchande a considérablement diminué. Comme il a été signalé dans *SoCalGas* :

> [TRADUCTION] Si la valeur du terrain devenait inférieure à son coût historique, on pourrait prétendre que le rendement constant versé au fil des ans [par les clients] pour le terrain a en fait surindemnisé les investisseurs. Le rapport entre les risques et les avantages est tout aussi symétrique pour un terrain que pour un bien amortissable lorsque leur coût est pris en compte pour l'établissement de la base tarifaire. [p. 107]

II. Conclusion

En résumé, le par. 15(3) de l'AEUBA conférait à la Commission le pouvoir d'[TRADUCTION] « imposer les conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public » en statuant sur la demande d'autorisation de la vente du terrain et des bâtiments en cause. Dans l'exercice de ce pouvoir, et vu la [TRADUCTION] « surveillance générale des services de gaz et de leurs propriétaires » qui lui incombait (GUA, par. 22(1)), la Commission a attribué le gain comme elle l'a fait pour les considérations d'intérêt public énoncées dans sa décision. Le pouvoir aurait peut-être été exercé différemment par un autre organisme de réglementation ou dans un autre ressort, mais il reste que la Commission était autorisée à répartir le gain tiré de la vente d'un bien qu'ATCO souhaitait soustraire à la base tarifaire. Il ne nous appartient pas de déterminer quelles conditions sont « nécessaires dans l'intérêt public » et de substituer notre opinion à celle de la Commission.

III. Dispositif

Je suis d'avis d'accueillir le pourvoi, d'annuler la décision de la Cour d'appel de l'Alberta et de rétablir la décision de la Commission, avec dépens payables à la ville de Calgary dans toutes les cours. Le pourvoi incident d'ATCO devrait être rejeté avec dépens.

APPENDIX

Alberta Energy and Utilities Board Act, R.S.A. 2000, c. A-17

Jurisdiction

13 All matters that may be dealt with by the ERCB or the PUB under any enactment or as otherwise provided by law shall be dealt with by the Board and are within the exclusive jurisdiction of the Board.

Powers of the Board

15(1) For the purposes of carrying out its functions, the Board has all the powers, rights and privileges of the ERCB and the PUB that are granted or provided for by any enactment or by law.

(2) In any case where the ERCB, the PUB or the Board may act in response to an application, complaint, direction, referral or request, the Board may act on its own initiative or motion.

(3) Without restricting subsection (1), the Board may do all or any of the following:

(a) make any order that the ERCB or the PUB may make under any enactment;

(b) with the approval of the Lieutenant Governor in Council, make any order that the ERCB may, with the approval of the Lieutenant Governor in Council, make under any enactment;

(c) with the approval of the Lieutenant Governor in Council, make any order that the PUB may, with the approval of the Lieutenant Governor in Council, make under any enactment;

(d) with respect to an order made by the Board, the ERCB or the PUB in respect of matters referred to in clauses (a) to (c), make any further order and impose any additional conditions that the Board considers necessary in the public interest;

(e) make an order granting the whole or part only of the relief applied for;

(f) where it appears to the Board to be just and proper, grant partial, further or other relief in

ANNEXE

Alberta Energy and Utilities Board Act, R.S.A. 2000, ch. A-17

[TRADUCTION]

Compétence

13 La Commission connaît de toute question dont peut connaître l'ERCB ou la PUB suivant un texte législatif ou le droit par ailleurs applicable, et sa compétence est exclusive.

Pouvoirs de la Commission

15(1) Dans l'exercice de ses fonctions, la Commission jouit des pouvoirs, des droits et des privilèges qu'un texte législatif ou le droit par ailleurs applicable confère à l'ERCB et à la PUB.

(2) La Commission peut agir d'office à l'égard de tout renvoi, demande, plainte, directive ou requête auquel l'ERCB, la PUB ou la Commission peut donner suite.

(3) Sans limiter la portée du paragraphe (1), la Commission peut prendre les mesures suivantes, en totalité ou en partie :

a) rendre toute ordonnance que l'ERCB ou la PUB peut rendre suivant un texte législatif;

b) avec l'approbation du lieutenant-gouverneur en conseil, rendre toute ordonnance que l'ERCB peut, avec l'approbation du lieutenant-gouverneur en conseil, rendre en vertu d'un texte législatif;

c) avec l'approbation du lieutenant-gouverneur en conseil, rendre toute ordonnance que la PUB peut, avec l'approbation du lieutenant-gouverneur en conseil, rendre en vertu d'un texte législatif;

d) à l'égard d'une ordonnance rendue par elle, l'ERCB ou la PUB en application des alinéas a) à c), rendre toute autre ordonnance et imposer les conditions supplémentaires qu'elle juge nécessaires dans l'intérêt public;

e) rendre une ordonnance accordant en tout ou en partie la réparation demandée;

f) lorsqu'elle l'estime juste et convenable, accorder en partie la réparation demandée ou en accorder

addition to, or in substitution for, that applied for as fully and in all respects as if the application or matter had been for that partial, further or other relief.

Appeals

26(1) Subject to subsection (2), an appeal lies from the Board to the Court of Appeal on a question of jurisdiction or on a question of law.

(2) Leave to appeal may be obtained from a judge of the Court of Appeal only on an application made

(a) within 30 days from the day that the order, decision or direction sought to be appealed from was made, or

(b) within a further period of time as granted by the judge where the judge is of the opinion that the circumstances warrant the granting of that further period of time.

. . .

Exclusion of prerogative writs

27 Subject to section 26, every action, order, ruling or decision of the Board or the person exercising the powers or performing the duties of the Board is final and shall not be questioned, reviewed or restrained by any proceeding in the nature of an application for judicial review or otherwise in any court.

Gas Utilities Act, R.S.A. 2000, c. G-5

Supervision

22(1) The Board shall exercise a general supervision over all gas utilities, and the owners of them, and may make any orders regarding equipment, appliances, extensions of works or systems, reporting and other matters, that are necessary for the convenience of the public or for the proper carrying out of any contract, charter or franchise involving the use of public property or rights.

(2) The Board shall conduct all inquiries necessary for the obtaining of complete information as to the manner in which owners of gas utilities comply with the law, or as to any other matter or thing within the jurisdiction of the Board under this Act.

une autre en sus ou en lieu et place comme si tel était l'objet de la demande.

Appel

26(1) Sous réserve du paragraphe (2), les décisions de la Commission sont susceptibles d'appel devant la Cour d'appel sur une question de droit ou de compétence.

(2) L'autorisation d'appel ne peut être obtenue d'un juge de la Cour d'appel que sur demande présentée

a) dans les 30 jours qui suivent l'ordonnance, la décision ou la directive en cause ou

b) dans le délai supplémentaire que le juge estime justifié d'accorder dans les circonstances.

. . .

Immunité de contrôle

27 Sous réserve de l'article 26, toute mesure, ordonnance ou décision de la Commission ou de la personne exerçant ses pouvoirs ou ses fonctions est définitive et ne peut être contestée, révisée ou restreinte dans le cadre d'une instance judiciaire, y compris une demande de contrôle judiciaire.

Gas Utilities Act, R.S.A. 2000, ch. G-5

[TRADUCTION]

Surveillance

22(1) La Commission assure la surveillance générale des services de gaz et de leurs propriétaires et peut, en ce qui concerne notamment le matériel, les appareils, les extensions d'ouvrages ou de systèmes et l'établissement de rapports, rendre les ordonnances nécessaires à la protection de l'intérêt public ou à la bonne application d'un contrat, de statuts constitutifs ou d'une concession comportant l'emploi de biens publics ou l'exercice de droits publics.

(2) La Commission mène toute enquête nécessaire à l'obtention de renseignements complets sur la façon dont le propriétaire d'un service de gaz se conforme à la loi ou sur tout ce qui est par ailleurs de son ressort suivant la présente loi.

Investigation of gas utility

24(1) The Board, on its own initiative or on the application of a person having an interest, may investigate any matter concerning a gas utility.

. . .

Designated gas utilities

26(1) The Lieutenant Governor in Council may by regulation designate those owners of gas utilities to which this section and section 27 apply.

(2) No owner of a gas utility designated under subsection (1) shall

(a) issue any

(i) of its shares or stock, or

(ii) bonds or other evidences of indebtedness, payable in more than one year from the date of them,

unless it has first satisfied the Board that the proposed issue is to be made in accordance with law and has obtained the approval of the Board for the purposes of the issue and an order of the Board authorizing the issue,

(b) capitalize

(i) its right to exist as a corporation,

(ii) a right, franchise or privilege in excess of the amount actually paid to the Government or a municipality as the consideration for it, exclusive of any tax or annual charge, or

(iii) a contract for consolidation, amalgamation or merger,

(c) without the approval of the Board, capitalize any lease, or

(d) without the approval of the Board,

(i) sell, lease, mortgage or otherwise dispose of or encumber its property, franchises, privileges or rights, or any part of it or them, or

(ii) merge or consolidate its property, franchises, privileges or rights, or any part of it or them,

Enquêtes

24(1) La Commission peut, d'office ou à la demande d'un intéressé, faire enquête sur toute question relative à un service de gaz.

. . .

Services de gaz désignés

26(1) Le lieutenant-gouverneur en conseil peut, par règlement, désigner les propriétaires de services de gaz assujettis au présent article et à l'article 27.

(2) Le propriétaire d'un service de gaz désigné en application du paragraphe (1) ne peut

a) émettre

(i) d'actions,

(ii) d'obligations ou d'autres titres d'emprunt dont le terme est supérieur à un an,

que si, au préalable, il convainc la Commission que l'émission projetée est conforme à la loi et obtient d'elle l'autorisation d'y procéder et une ordonnance le confirmant;

b) capitaliser

(i) son droit d'exister en tant que personne morale,

(ii) un droit, une concession ou un privilège en sus du montant réellement versé en contrepartie à l'État ou à une municipalité, à l'exclusion d'une taxe ou d'une charge annuelle,

(iii) un contrat de fusion ou de regroupement;

c) sans l'autorisation de la Commission, capitaliser un bail;

d) sans l'autorisation de la Commission,

(i) aliéner ou grever ses biens, concessions, privilèges ou droits, en tout ou en partie, notamment en les vendant, en les louant ou en les hypothéquant,

(ii) fusionner ou regrouper ses biens, concessions, privilèges ou droits, en tout ou en partie;

and a sale, lease, mortgage, disposition, encumbrance, merger or consolidation made in contravention of this clause is void, but nothing in this clause shall be construed to prevent in any way the sale, lease, mortgage, disposition, encumbrance, merger or consolidation of any of the property of an owner of a gas utility designated under subsection (1) in the ordinary course of the owner's business.

. . .

Prohibited share transactions

27(1) Unless authorized to do so by an order of the Board, the owner of a gas utility designated under section 26(1) shall not sell or make or permit to be made on its books any transfer of any share or shares of its capital stock to a corporation, however incorporated, if the sale or transfer, by itself or in connection with previous sales or transfers, would result in the vesting in that corporation of more than 50% of the outstanding capital stock of the owner of the gas utility.

. . .

Powers of Board

36 The Board, on its own initiative or on the application of a person having an interest, may by order in writing, which is to be made after giving notice to and hearing the parties interested,

(a) fix just and reasonable individual rates, joint rates, tolls or charges or schedules of them, as well as commutation and other special rates, which shall be imposed, observed and followed afterwards by the owner of the gas utility,

(b) fix proper and adequate rates and methods of depreciation, amortization or depletion in respect of the property of any owner of a gas utility, who shall make the owner's depreciation, amortization or depletion accounts conform to the rates and methods fixed by the Board,

(c) fix just and reasonable standards, classifications, regulations, practices, measurements or service, which shall be furnished, imposed, observed and followed thereafter by the owner of the gas utility,

(d) require an owner of a gas utility to establish, construct, maintain and operate, but in

tout grèvement, vente, location, constitution d'hypothèque, aliénation, regroupement ou fusion intervenant en contravention de la présente disposition est nul, sauf s'il intervient dans le cours normal des activités de l'entreprise.

. . .

Incessibilité des actions

27(1) Sauf ordonnance de la Commission l'y autorisant, le propriétaire d'un service de gaz désigné en application du paragraphe 26(1) s'abstient de vendre tout ou partie des actions de son capital-actions à une société, indépendamment du mode de constitution de celle-ci, ou d'effectuer ou d'autoriser une inscription dans ses registres constatant une telle cession, lorsque la vente ou la cession, à elle seule ou de pair avec une opération antérieure, ferait en sorte que la société détienne plus de 50 % des actions en circulation du propriétaire du service de gaz.

. . .

Pouvoirs de la Commission

36 La Commission peut, d'office ou à la demande d'un intéressé, par ordonnance écrite, après avoir donné un avis aux personnes intéressées et les avoir entendues,

a) fixer des tarifs individuels ou conjoints, des taux ou des charges justes et raisonnables, ou leurs barèmes, ainsi que des tarifs d'abonnement et d'autres tarifs spéciaux opposables au propriétaire d'un service de gaz et applicables par lui;

b) établir des taux et des méthodes valables et acceptables de dépréciation, d'amortissement et d'épuisement pour les biens du propriétaire d'un service de gaz, qui doit s'y conformer dans la tenue des comptes y afférents;

c) à l'intention du propriétaire d'un service de gaz, établir des normes, des classifications, des règles, des pratiques ou des mesures justes et raisonnables et déterminer les services justes et raisonnables devant être fournis;

d) exiger que le propriétaire d'un service de gaz construise, entretienne et exploite,

compliance with this and any other Act relating to it, any reasonable extension of the owner's existing facilities when in the judgment of the Board the extension is reasonable and practical and will furnish sufficient business to justify its construction and maintenance, and when the financial position of the owner of the gas utility reasonably warrants the original expenditure required in making and operating the extension, and

(e) require an owner of a gas utility to supply and deliver gas to the persons, for the purposes, at the rates, prices and charges and on the terms and conditions that the Board directs, fixes or imposes.

Rate base

37(1) In fixing just and reasonable rates, tolls or charges, or schedules of them, to be imposed, observed and followed afterwards by an owner of a gas utility, the Board shall determine a rate base for the property of the owner of the gas utility used or required to be used to provide service to the public within Alberta and on determining a rate base it shall fix a fair return on the rate base.

(2) In determining a rate base under this section, the Board shall give due consideration

(a) to the cost of the property when first devoted to public use and to prudent acquisition cost to the owner of the gas utility, less depreciation, amortization or depletion in respect of each, and

(b) to necessary working capital.

(3) In fixing the fair return that an owner of a gas utility is entitled to earn on the rate base, the Board shall give due consideration to all facts that in its opinion are relevant.

Excess revenues or losses

40 In fixing just and reasonable rates, tolls or charges, or schedules of them, to be imposed, observed and followed afterwards by an owner of a gas utility,

(a) the Board may consider all revenues and costs of the owner that are in the Board's opinion applicable to a period consisting of

(i) the whole of the fiscal year of the owner in which a proceeding is initiated for the

conformément à la présente loi et à toute autre s'y rapportant, une extension raisonnable de ses installations lorsqu'elle juge que cette extension est raisonnable et réalisable, que les prévisions de rentabilité justifient sa construction et son entretien et que la situation financière du propriétaire du service de gaz justifie raisonnablement les dépenses initiales requises pour construire et exploiter l'extension;

e) exiger que le propriétaire d'un service de gaz approvisionne en gaz certaines personnes, à certaines fins, en contrepartie de certains tarifs, prix et charges, et à certaines conditions, selon ce qu'elle détermine.

Base tarifaire

37(1) Pour fixer des tarifs, des taux ou des charges justes et raisonnables, ou leurs barèmes, opposables au propriétaire d'un service de gaz et applicables par lui, la Commission établit une base tarifaire pour les biens du propriétaire d'un service de gaz servant ou devant servir à la fourniture du service au public en Alberta et, ce faisant, elle établit un juste rendement.

(2) Pour établir la base tarifaire, la Commission tient compte

a) du coût du bien lors de son affectation initiale à l'utilisation publique et de sa juste valeur d'acquisition pour le propriétaire du service de gaz, moins la dépréciation, l'amortissement et l'épuisement;

b) du capital nécessaire.

(3) Pour établir le juste rendement auquel a droit le propriétaire d'un service de gaz par rapport à la base tarifaire, la Commission tient compte de tous les facteurs qu'elle estime pertinents.

Recettes excédentaires ou insuffisantes

40 Pour fixer des tarifs, des taux ou des charges justes et raisonnables, ou leurs barèmes, opposables au propriétaire d'un service de gaz et applicables par lui, la Commission

a) peut tenir compte de toutes les recettes et les dépenses du propriétaire qu'elle estime afférentes à l'une des périodes suivantes, à l'exclusion de toute attribution à une partie de cette période :

(i) la totalité de l'exercice du propriétaire au cours duquel est engagée une procédure de

fixing of rates, tolls or charges, or schedules of them,

(ii) a subsequent fiscal year of the owner, or

(iii) 2 or more of the fiscal years of the owner referred to in subclauses (i) and (ii) if they are consecutive,

and need not consider the allocation of those revenues and costs to any part of that period,

(b) the Board may give effect to that part of any excess revenue received or any revenue deficiency incurred by the owner that is in the Board's opinion applicable to the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them, that the Board determines is just and reasonable,

(c) the Board may give effect to that part of any excess revenue received or any revenue deficiency incurred by the owner after the date on which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them, that the Board determines has been due to undue delay in the hearing and determining of the matter, and

(d) the Board shall by order approve

(i) the method by which, and

(ii) the period, including any subsequent fiscal period, during which,

any excess revenue received or any revenue deficiency incurred, as determined pursuant to clause (b) or (c), is to be used or dealt with.

General powers of Board

59 For the purposes of this Act, the Board has the same powers in respect of the plant, premises, equipment, service and organization for the production, distribution and sale of gas in Alberta, and in respect of the business of an owner of a gas utility and in respect of an owner of a gas utility, that are by the *Public Utilities Board Act* conferred on the Board in the case of a public utility under that Act.

Public Utilities Board Act, R.S.A. 2000, c. P-45

Jurisdiction and powers

36(1) The Board has all the necessary jurisdiction and power

fixation des tarifs, des taux ou des charges, ou de leurs barèmes,

(ii) un exercice ultérieur,

(iii) deux exercices ou plus visés aux sous-alinéas (i) et (ii), s'ils sont consécutifs;

b) peut prendre en considération la partie de l'excédent ou du déficit du propriétaire qui, selon elle, se rattache à la totalité de l'exercice du propriétaire au cours duquel est engagée une procédure de fixation de tarifs, de taux et de charges, ou de leurs barèmes, qu'elle estime justes et raisonnables;

c) peut prendre en considération la partie de l'excédent ou du déficit du propriétaire subséquent au début de la procédure visée à l'alinéa b) qui, selon elle, est attribuable à un retard injustifié dans le déroulement de la procédure;

d) approuve par ordonnance ce qu'il convient de faire de tout excédent ou déficit visé aux alinéas b) ou c) et la période, y compris tout exercice ultérieur, au cours de laquelle il convient de le faire.

Pouvoirs généraux

59 Pour l'application de la présente loi, la Commission a, à l'égard des installations, des locaux, du matériel, des services, de l'organisation de la production, de la distribution et de la vente de gaz en Alberta, ainsi que du propriétaire d'un service de gaz et de son entreprise, les pouvoirs que lui confère la *Public Utilities Board Act* à l'égard d'une entreprise de services publics au sens de cette loi.

Public Utilities Board Act, R.S.A. 2000, ch. P-45

[TRADUCTION]

Compétence et pouvoirs

36(1) La Commission a la compétence et les pouvoirs nécessaires

(a) to deal with public utilities and the owners of them as provided in this Act;

(b) to deal with public utilities and related matters as they concern suburban areas adjacent to a city, as provided in this Act.

(2) In addition to the jurisdiction and powers mentioned in subsection (1), the Board has all necessary jurisdiction and powers to perform any duties that are assigned to it by statute or pursuant to statutory authority.

(3) The Board has, and is deemed at all times to have had, jurisdiction to fix and settle, on application, the price and terms of purchase by a council of a municipality pursuant to section 47 of the *Municipal Government Act*

(a) before the exercise by the council under that provision of its right to purchase and without binding the council to purchase, or

(b) when an application is made under that provision for the Board's consent to the purchase, before hearing or determining the application for its consent.

General power

37 In matters within its jurisdiction the Board may order and require any person or local authority to do forthwith or within or at a specified time and in any manner prescribed by the Board, so far as it is not inconsistent with this Act or any other Act conferring jurisdiction, any act, matter or thing that the person or local authority is or may be required to do under this Act or under any other general or special Act, and may forbid the doing or continuing of any act, matter or thing that is in contravention of any such Act or of any regulation, rule, order or direction of the Board.

Investigation of utilities and rates

80 When it is made to appear to the Board, on the application of an owner of a public utility or of a municipality or person having an interest, present or contingent, in the matter in respect of which the application is made, that there is reason to believe that the tolls demanded by an owner of a public utility exceed what is just and reasonable, having regard to the nature and quality of the service rendered or of the commodity supplied, the Board

(a) may proceed to hold any investigation that it thinks fit into all matters relating to the nature

a) pour agir à l'égard des entreprises de services publics et de leurs propriétaires conformément à la présente loi;

b) pour agir à l'égard des entreprises de services publics et connaître de questions connexes touchant une région adjacente à une ville, conformément à la présente loi.

(2) Outre la compétence et les pouvoirs mentionnés au paragraphe (1), la Commission a la compétence et les pouvoirs nécessaires pour exercer les fonctions qui lui sont légalement dévolues.

(3) La Commission a et est réputée avoir toujours eu compétence pour fixer, sur demande, le prix et les conditions d'une acquisition effectuée par un conseil municipal sous le régime de l'article 47 de la *Municipal Government Act*

a) avant que le conseil n'exerce son droit d'acquisition suivant cet article, et sans qu'il soit tenu de procéder à l'acquisition ou

b) lorsque l'acquisition est soumise à son approbation suivant cet article, avant que la Commission n'entende la demande et ne statue sur elle.

Pouvoirs généraux

37 Dans les domaines de sa compétence, la Commission peut ordonner et exiger qu'une personne, y compris une administration municipale, immédiatement ou dans le délai qu'elle impartit et selon les modalités qu'elle détermine, à condition que ce ne soit pas incompatible avec la présente loi ou une autre conférant compétence, fasse ce qu'elle est tenue de faire ou susceptible d'être tenue de faire suivant la présente loi ou toute autre, générale ou spéciale, et elle peut interdire ou faire cesser tout ce qui contrevient à ces lois ou à ses règles, ses ordonnances ou ses directives.

Enquêtes sur les services publics et les tarifs

80 Lorsqu'il lui est démontré à l'audition d'une demande présentée par le propriétaire d'une entreprise de services publics ou par une municipalité ou une personne ayant un intérêt actuel ou éventuel dans l'objet de la demande, qu'il y a lieu de croire que les taux établis par le propriétaire d'une entreprise de services publics excèdent ce qui est juste et raisonnable eu égard à la nature et à la qualité du service ou du produit en cause, la Commission

a) peut enquêter comme elle le juge utile sur toute question liée à la nature et à la qualité du

and quality of the service or the commodity in question, or to the performance of the service and the tolls or charges demanded for it,

(b) may make any order respecting the improvement of the service or commodity and as to the tolls or charges demanded, that seems to it to be just and reasonable, and

(c) may disallow or change, as it thinks reasonable, any such tolls or charges that, in its opinion, are excessive, unjust or unreasonable or unjustly discriminate between different persons or different municipalities, but subject however to any provisions of any contract existing between the owner of the public utility and a municipality at the time the application is made that the Board considers fair and reasonable.

Supervision by Board

85(1) The Board shall exercise a general supervision over all public utilities, and the owners of them, and may make any orders regarding extension of works or systems, reporting and other matters, that are necessary for the convenience of the public or for the proper carrying out of any contract, charter or franchise involving the use of public property or rights.

. . .

Investigation of public utility

87(1) The Board may, on its own initiative, or on the application of a person having an interest, investigate any matter concerning a public utility.

(2) When in the opinion of the Board it is necessary to investigate a public utility or the affairs of its owner, the Board shall be given access to and may use any books, documents or records with respect to the public utility and in the possession of any owner of the public utility or municipality or under the control of a board, commission or department of the Government.

(3) A person who directly or indirectly controls the business of an owner of a public utility within Alberta and any company controlled by that person shall give the Board or its agent access to any of the books, documents and records that relate to the business of the owner or shall furnish any information in respect of it required by the Board.

service ou du produit en cause, ou à l'exécution du service et aux taux ou charges y afférents;

b) peut, en ce qui concerne l'amélioration du service ou du produit et les taux et charges y afférents, rendre toute ordonnance qu'elle estime juste et raisonnable;

c) peut écarter ou modifier, comme elle l'estime raisonnable, les taux ou les charges qu'elle juge excessifs, injustes ou déraisonnables, ou indûment discriminatoires envers une personne, y compris une municipalité, sous réserve toutefois des dispositions qu'elle considère justes et raisonnables d'un contrat liant le propriétaire de l'entreprise de services publics et une municipalité au moment de la demande.

Surveillance

85(1) La Commission assure la surveillance générale des entreprises de services publics et de leurs propriétaires et peut, en ce qui concerne notamment les extensions d'ouvrages ou de systèmes et l'établissement de rapports, rendre les ordonnances nécessaires à la protection de l'intérêt public ou à la bonne exécution d'un contrat, de statuts constitutifs ou d'une concession comportant l'emploi de biens publics ou l'exercice de droits publics.

. . .

Enquêtes

87(1) La Commission peut, d'office ou à la demande d'un intéressé, faire enquête sur toute question relative à une entreprise de services publics.

(2) Lorsqu'elle estime nécessaire d'enquêter sur une entreprise de services publics ou sur les activités de son propriétaire, la Commission a accès aux livres, documents et dossiers relatifs à l'entreprise qui sont en la possession du propriétaire, d'une municipalité, d'un organisme public ou d'un ministère, et elle peut les utiliser.

(3) La personne qui exerce un pouvoir direct ou indirect sur l'entreprise d'un propriétaire de services publics en Alberta et toute société dont cette personne est actionnaire majoritaire est tenue de donner à la Commission ou à son représentant l'accès aux livres, documents et dossiers relatifs à l'entreprise du propriétaire ou de communiquer tout renseignement y afférent exigé par la Commission.

Fixing of rates

89 The Board, either on its own initiative or on the application of a person having an interest, may by order in writing, which is to be made after giving notice to and hearing the parties interested,

(a) fix just and reasonable individual rates, joint rates, tolls or charges, or schedules of them, as well as commutation, mileage or kilometre rate and other special rates, which shall be imposed, observed and followed subsequently by the owner of the public utility;

(b) fix proper and adequate rates and methods of depreciation, amortization or depletion in respect of the property of any owner of a public utility, who shall make the owner's depreciation, amortization or depletion accounts conform to the rates and methods fixed by the Board;

(c) fix just and reasonable standards, classifications, regulations, practices, measurements or service, which shall be furnished, imposed, observed and followed subsequently by the owner of the public utility;

(d) repealed;

(e) require an owner of a public utility to establish, construct, maintain and operate, but in compliance with other provisions of this or any other Act relating to it, any reasonable extension of the owner's existing facilities when in the judgment of the Board the extension is reasonable and practical and will furnish sufficient business to justify its construction and maintenance, and when the financial position of the owner of the public utility reasonably warrants the original expenditure required in making and operating the extension.

Determining rate base

90(1) In fixing just and reasonable rates, tolls or charges, or schedules of them, to be imposed, observed and followed subsequently by an owner of a public utility, the Board shall determine a rate base for the property of the owner of a public utility used or required to be used to provide service to the public within Alberta and on determining a rate base it shall fix a fair return on the rate base.

(2) In determining a rate base under this section, the Board shall give due consideration

(a) to the cost of the property when first devoted to public use and to prudent acquisition cost to

Établissement des tarifs

89 La Commission peut, d'office ou à la demande d'un intéressé, par ordonnance écrite, après avoir donné un avis aux personnes intéressées et les avoir entendues,

a) fixer des tarifs individuels ou conjoints, des taux ou des charges justes et raisonnables, ou leurs barèmes, ainsi que des tarifs d'abonnement, des tarifs au mille ou au kilomètre et d'autres tarifs spéciaux opposables au propriétaire de l'entreprise de services publics et applicables par lui;

b) établir des taux et des méthodes valables et acceptables de dépréciation, d'amortissement et d'épuisement pour les biens du propriétaire d'une entreprise de services publics, qui doit s'y conformer dans la tenue des comptes y afférents;

c) à l'intention du propriétaire d'une entreprise de services publics, établir des normes, des classifications, des règles, des pratiques ou des mesures justes et raisonnables et déterminer les services justes et raisonnables devant être fournis;

d) abrogé;

e) exiger qu'un propriétaire d'entreprise de services publics construise, entretienne et exploite, conformément à toute autre disposition de la présente loi ou d'une autre s'y rapportant, une extension raisonnable de ses installations lorsqu'elle juge que cette extension est raisonnable et réalisable, que les prévisions de rentabilité justifient sa construction et son entretien et que la situation financière du propriétaire de l'entreprise de services publics justifie raisonnablement les dépenses initiales requises pour construire et exploiter l'extension.

Base tarifaire

90(1) Pour fixer des tarifs, des taux ou des charges justes et raisonnables, ou leurs barèmes, opposables au propriétaire d'une entreprise de services public et applicables par lui, la Commission établit une base tarifaire pour les biens du propriétaire de l'entreprise de services publics servant ou devant servir à la fourniture du service au public en Alberta et, ce faisant, elle établit un juste rendement.

(2) Pour établir la base tarifaire, la Commission tient compte :

a) du coût du bien lors de son affectation initiale à l'utilisation publique et de sa juste valeur

the owner of the public utility, less depreciation, amortization or depletion in respect of each, and

(b) to necessary working capital.

(3) In fixing the fair return that an owner of a public utility is entitled to earn on the rate base, the Board shall give due consideration to all those facts that, in the Board's opinion, are relevant.

Revenue and costs considered

91(1) In fixing just and reasonable rates, tolls or charges, or schedules of them, to be imposed, observed and followed by an owner of a public utility,

(a) the Board may consider all revenues and costs of the owner that are in the Board's opinion applicable to a period consisting of

(i) the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them,

(ii) a subsequent fiscal year of the owner, or

(iii) 2 or more of the fiscal years of the owner referred to in subclauses (i) and (ii) if they are consecutive,

and need not consider the allocation of those revenues and costs to any part of such a period,

(b) the Board shall consider the effect of the *Small Power Research and Development Act* on the revenues and costs of the owner with respect to the generation, transmission and distribution of electric energy,

(c) the Board may give effect to that part of any excess revenue received or any revenue deficiency incurred by the owner that is in the Board's opinion applicable to the whole of the fiscal year of the owner in which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them, as the Board determines is just and reasonable,

(d) the Board may give effect to such part of any excess revenue received or any revenue deficiency incurred by the owner after the date on which a proceeding is initiated for the fixing of rates, tolls or charges, or schedules of them, as the Board determines has been due to undue delay in the hearing and determining of the matter, and

d'acquisition pour le propriétaire de l'entreprise de services publics, moins la dépréciation, l'amortissement et l'épuisement;

b) du capital nécessaire.

(3) Pour établir le juste rendement auquel a droit le propriétaire d'une entreprise de services publics par rapport à la base tarifaire, la Commission tient compte de tous les facteurs qui, selon elle, sont pertinents.

Prise en compte des recettes et des dépenses

91(1) Pour fixer des tarifs, des taux ou des charges justes et raisonnables, ou leurs barèmes, opposables au propriétaire d'une entreprise de services publics et applicables par lui, la Commission

a) peut tenir compte de toutes les recettes et les dépenses du propriétaire qu'elle estime afférentes à l'une des périodes suivantes, à l'exclusion de toute attribution à une partie de cette période :

(i) la totalité de l'exercice du propriétaire au cours duquel est engagée une procédure de fixation des tarifs, des taux ou des charges, ou de leurs barèmes;

(ii) un exercice ultérieur;

(iii) deux exercices ou plus visés aux sous-alinéas (i) et (ii), s'ils sont consécutifs;

b) tient compte de l'incidence de la *Small Power Research and Development Act* sur les recettes et les dépenses du propriétaire relatives à la production, au transport et à la distribution d'électricité;

c) peut prendre en considération la partie de l'excédent ou du déficit du propriétaire qui, selon elle, se rattache à la totalité de l'exercice du propriétaire au cours duquel est engagée une procédure de fixation de tarifs, de taux et de charges, ou de leurs barèmes, qu'elle estime justes et raisonnables;

d) peut prendre en considération la partie de l'excédent ou du déficit du propriétaire subséquent au début de la procédure visée à l'alinéa c) qui, selon elle, est attribuable à un retard injustifié dans le déroulement de la procédure;

(e) the Board shall by order approve the method by which, and the period (including any subsequent fiscal period) during which, any excess revenue received or any revenue deficiency incurred, as determined pursuant to clause (c) or (d), is to be used or dealt with.

Designated public utilities

101(1) The Lieutenant Governor in Council may by regulation designate those owners of public utilities to which this section and section 102 apply.

(2) No owner of a public utility designated under subsection (1) shall

(a) issue any

(i) of its shares or stock, or

(ii) bonds or other evidences of indebtedness, payable in more than one year from the date of them,

unless it has first satisfied the Board that the proposed issue is to be made in accordance with law and has obtained the approval of the Board for the purposes of the issue and an order of the Board authorizing the issue,

(b) capitalize

(i) its right to exist as a corporation,

(ii) a right, franchise or privilege in excess of the amount actually paid to the Government or a municipality as the consideration for it, exclusive of any tax or annual charge, or

(iii) a contract for consolidation, amalgamation or merger,

(c) without the approval of the Board, capitalize any lease, or

(d) without the approval of the Board,

(i) sell, lease, mortgage or otherwise dispose of or encumber its property, franchises, privileges or rights, or any part of them, or

(ii) merge or consolidate its property, franchises, privileges or rights, or any part of them,

e) approuve par ordonnance ce qu'il convient de faire de tout excédent ou déficit visé aux alinéas c) ou d) et la période (y compris tout exercice ultérieur) au cours de laquelle il convient de le faire.

Services de gaz désignés

101(1) Le lieutenant-gouverneur en conseil peut, par règlement, désigner les propriétaires d'entreprises de services publics assujettis au présent article et à l'article 102.

(2) Le propriétaire d'une entreprise de services publics désigné en application du paragraphe (1) ne peut

a) émettre

(i) d'actions,

(ii) d'obligations ou d'autres titres d'emprunt dont le terme est supérieur à un an,

que si, au préalable, il convainc la Commission que l'émission projetée est conforme à la loi et obtient d'elle l'autorisation d'y procéder et une ordonnance le confirmant;

b) capitaliser

(i) son droit d'exister en tant que personne morale,

(ii) un droit, une concession ou un privilège en sus du montant réellement versé en contrepartie à l'État ou à une municipalité, à l'exclusion d'une taxe ou d'une charge annuelle,

(iii) un contrat de fusion ou de regroupement;

c) sans l'autorisation de la Commission, capitaliser un bail;

d) sans l'autorisation de la Commission,

(i) aliéner ou grever ses biens, concessions, privilèges ou droits, en tout ou en partie, notamment en les vendant, en les louant ou en les hypothéquant,

(ii) fusionner ou regrouper ses biens, concessions, privilèges ou droits, en tout ou en partie;

and a sale, lease, mortgage, disposition, encumbrance, merger or consolidation made in contravention of this clause is void, but nothing in this clause shall be construed to prevent in any way the sale, lease, mortgage, disposition, encumbrance, merger or consolidation of any of the property of an owner of a public utility designated under subsection (1) in the ordinary course of the owner's business.

. . .

Prohibited share transaction

102(1) Unless authorized to do so by an order of the Board, the owner of a public utility designated under section 101(1) shall not sell or make or permit to be made on its books a transfer of any share of its capital stock to a corporation, however incorporated, if the sale or transfer, in itself or in connection with previous sales or transfers, would result in the vesting in that corporation of more than 50% of the outstanding capital stock of the owner of the public utility.

. . .

Interpretation Act, R.S.A. 2000, c. I-8

Enactments remedial

10 An enactment shall be construed as being remedial, and shall be given the fair, large and liberal construction and interpretation that best ensures the attainment of its objects.

Appeal dismissed with costs and cross-appeal allowed with costs, McLachlin C.J. *and* Binnie *and* Fish JJ. *dissenting.*

Solicitors for the appellant/respondent on cross-appeal: McLennan Ross, Calgary.

Solicitors for the respondent/appellant on cross-appeal: Bennett Jones, Calgary.

Solicitor for the intervener the Alberta Energy and Utilities Board: J. Richard McKee, Calgary.

tout grèvement, vente, location, constitution d'hypothèque, aliénation, regroupement ou fusion intervenant en contravention de la présente disposition est nul, sauf s'il intervient dans le cours normal des activités de l'entreprise.

. . .

Incessibilité des actions

102(1) Sauf ordonnance de la Commission l'y autorisant, le propriétaire d'une entreprise de services publics désignée en application du paragraphe 101(1) s'abstient de vendre tout ou partie des actions de son capital-actions à une société, indépendamment du mode de constitution de celle-ci, ou d'effectuer ou d'autoriser une inscription dans ses registres constatant une telle cession, lorsque la vente ou la cession, à elle seule ou de pair avec une opération antérieure, ferait en sorte que la société détienne plus de 50 % des actions en circulation du propriétaire de l'entreprise de services publics.

. . .

Interpretation Act, R.S.A. 2000, ch. I-8

[TRADUCTION]

Principe et interprétation

10 Tout texte est réputé apporter une solution de droit et s'interprète de la manière la plus équitable et la plus large qui soit compatible avec la réalisation de son objet.

Pourvoi rejeté avec dépens et pourvoi incident accueilli avec dépens, la juge en chef McLachlin *et les juges* Binnie *et* Fish *sont dissidents.*

Procureurs de l'appelante/intimée au pourvoi incident : McLennan Ross, Calgary.

Procureurs de l'intimée/appelante au pourvoi incident : Bennett Jones, Calgary.

Procureur de l'intervenante Alberta Energy and Utilities Board : J. Richard McKee, Calgary.

Solicitor for the intervener the Ontario Energy Board: Ontario Energy Board, Toronto.

Solicitors for the intervener Enbridge Gas Distribution Inc.: Fraser Milner Casgrain, Toronto.

Solicitors for the intervener Union Gas Limited: Torys, Toronto.

Procureur de l'intervenante la Commission de l'énergie de l'Ontario : Commission de l'énergie de l'Ontario, Toronto.

Procureurs de l'intervenante Enbridge Gas Distribution Inc. : Fraser Milner Casgrain, Toronto.

Procureurs de l'intervenante Union Gas Limited : Torys, Toronto.