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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.
Application Approval for Code of Conduct and Transfer Pricing Policy for Affiliated Regulated Businesses Operating in a Non-Natural Monopoly Environment

We enclose for filing in the above proceedings the electronic version of the Reply Submission on behalf of FortisBC Energy Inc. dated December 9, 2014, together with electronic copies of the judicial authorities cited.

Ten hard copies of the Reply Submission will follow by courier.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP

[original signed by Matthew Ghikas]

Matthew Ghikas

MTG/fxm
Encs

BRITISH COLUMBIA UTILITIES COMMISSION

IN THE MATTER OF THE UTILITIES COMMISSION ACT

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

and

FORTISBC ENERGY INC.
APPLICATION FOR APPROVAL OF CODE OF CONDUCT AND TRANSFER PRICING POLICY FOR AFFILIATED REGULATED BUSINESSES OPERATING IN A NON-NATURAL MONOPOLY ENVIRONMENT

REPLY SUBMISSION OF

FORTISBC ENERGY INC.

December 9, 2014

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PART ONE: INTRODUCTION

1. Interveners other than the competitors of FortisBC Alternative Energy Services Inc. (FAES) have generally supported FortisBC Energy Inc.'s (FEI) Application. They have echoed FEI's submission that the Commission owes both utilities (FEI and FAES) and their respective ratepayers a statutory duty to ensure that rates are just and reasonable. They also generally agree, with the exception of BCOAPO in the case of financing, that FEI has proposed a Code of Conduct (CoC) and a Transfer Pricing Policy (TPP) that best achieve the statutory objective of just and reasonable rates. Accordingly, the primary focus of FEI's Reply Submission is on responding to submissions of Corix and the Coalition.

2. FEI supports the adoption of CoC/TPP provisions that are reasonably necessary to safeguard the interests of its customers. The approach of the Coalition and Corix in this proceeding has been to propose CoC/TPP measures that are out of proportion to the risk or concern being addressed. Corix and the Coalition advance their positions safe in the knowledge that they would stand to benefit from inefficiencies imposed on FEI and FAES through unduly onerous provisions in the CoC and TPP. It is FEI, FAES and their respective customers who would end up living with the negative consequences of the positions advanced by Corix and the Coalition.[1] Significantly, it is these parties, and not FAES' competitors, to whom the Commission owes statutory duties in this context. FEI respectfully submits that the Commission should approve the Company's proposed CoC and TPP for the reasons set out in FEI's Final Submission and in this Reply Submission.

3. FEI's Reply Submission is organized to generally track FEI's Final Submission. As FEI's Reply Submission focuses on the primary arguments of Corix and the Coalition, FEI's silence on a particular issue should not be construed as agreement.

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[1] While Corix notes that it is also a customer of FEI, the price that Corix pays FEI for natural gas service is net neutral as it relates to Corix's market position because FAES also pays the same rates. Corix's submission patently advances its interests as a competitor of FAES.

PART TWO: GOVERNING LEGAL FRAMEWORK

4. Part Two responds to submissions of the Coalition and Corix regarding the legal framework (the other interveners were aligned with FEI). The Commission should reject the arguments of Corix and the Coalition, as their arguments are at odds with the UCA and case law.

A. DIFFERENT CONSIDERATIONS AT PLAY WITH TWO PUBLIC UTILITIES

5. The Coalition, in its "General Comments", states: "If an affiliate is in a 'non-natural monopoly environment', whether they are regulated (such as FAES) or a non-regulated businesses (sic) we suggest that this distinction does not warrant 'Code of Conduct' light."[2] There are two related answers to this argument:

- First, the Coalition's characterization of FEI's proposal as being "light" is inaccurate. The requirements are different, but FEI's proposed CoC/TPP framework for ARBNNMs is equally comprehensive and enforceable as the existing CoC/TPP for NRBs. The obligations are subject to compliance measures and oversight by the Commission. FEI has even proposed new compliance measures.

- Second, the requirements of the proposed COC/TPP *should* differ from the requirements governing FEI's relationship with NRBs because the nature of the relationship is different. The Commission does not owe statutory duties to a non-utility or its customers; the Commission's sole responsibility in the context of a utility-NRB interaction is to ensure that the rates of the one regulated utility are just and reasonable. In such circumstances, the Commission is not faced with having to weigh the interests of two regulated utility affiliates and their respective customers.

[2] Coalition Submission, para. 10.

B. NO JURISDICTION TO CONSIDER MARKET OUTCOMES

6. The Coalition maintains that "the Commission has a broader mandate as demonstrated by use of the words 'public interest' in a number of sections of the *Utilities Commission Act*"[3] and concludes that the Commission must therefore consider the customers of "a third party TES provider".[4] Corix similarly asserts that, by virtue of granting a CPCN to FEI, the Commission "has the mandate to consider how the public utility assets are used in the broader public context"[5] and that this mandate includes "ensur[ing] that FEI's use of natural gas utility resources does not hinder 'government energy objectives' and the development of the AES market."[6] FEI submits that these arguments must fail. As discussed below:

- First, there is no express language in the UCA conferring jurisdiction on the Commission to consider or promote TES market outcomes, and that jurisdiction cannot be implied by practical necessity.

- Second, their attempt to re-characterize consideration of market outcomes as overseeing the use of utility resources (Corix) or accounting for customers of other TES providers (Coalition) contravenes the administrative law principle precluding the Commission from regulating indirectly what it cannot regulate directly.

- Third, the Commission is exercising a rate setting function in establishing a CoC and TPP, not a broader public interest mandate.

(a) No Express or Implied Powers to Consider or Promote Market Outcomes

7. There is no express language in the UCA conferring jurisdiction on the Commission to consider or promote market outcomes, and that jurisdiction cannot be implied by practical necessity.

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[3] Coalition Submission, para. 10.

[4] Coalition Submission, para. 48.

[5] Corix Submission, para. 20.

[6] Corix Submission, para. 20.

Express and Implied Powers

8. The Commission is a creature of statute. The law is that "Statutory bodies to which specific powers are delegated may only deal with matters over which they have authority, and may not abuse that authority. They must always demonstrate that their actions are within 'the four corners of their jurisdiction', and fall squarely within the boundaries set by legislation."[7]

9. The "four corners" of the Commission's jurisdiction are determined by the express statutory language in the UCA, read in the context of the legislative purpose. In the absence of an explicit power, jurisdiction can only be implied from broadly worded provisions or otherwise to the extent that there is a "practical necessity" to achieve the legislative purpose. In *ATCO,* the Supreme Court of Canada considered a public interest power of ostensibly unlimited scope, and stated:

> 77 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.)).[8] [Emphasis added.]

10. The Commission has previously rejected the argument that examining the implications of a CoC/TPP on the wider market falls within its statutory mandate. It held in the RMDM Decision, for instance[9]:

> Conversely, the Commission finds that it has no jurisdiction to consider the impacts of the use of utility assets and services, either directly or through NRBs, on the retail market downstream of the meter. Accordingly, the fourth staff objective, that customer choice should be maximized, and the additional objective proposed by Enron, that robust competition in downstream markets should be preserved and enhanced, are beyond the responsibilities of the Commission in making its determinations.

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[7] G. Gegimbald, *Canadian Administrative Law* (1st), p. 144.

[8] See also: *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board),* 2006 SCC 4, para. 51.

[9] RMDM Decision, p. 22.

> With respect to the third objective identified by staff, that the most efficient allocation of goods and resources should be sought, the Commission believes that this forms a proper part of its consideration, but only to the extent that ratepayers are affected. Accordingly, the Commission believes that it may consider whether a proposal would enhance or reduce the possibility of stranded utility assets, or otherwise increase the economic efficiency with which utility assets are used for the benefit of ratepayers, but may not consider the implications for economic efficiency with respect to the larger market. The Commission accepts the concern voiced by some parties that a precise measurement of economic efficiency is not possible, particularly when considered from a societal perspective, but expects that it is possible to determine directionally whether a particular proposal enhances or reduces the likelihood of stranded costs or otherwise provides benefits to ratepayers. [Emphasis added.]

11. The Commission's articulation of its jurisdiction in the above passage is correct based on accepted principles of statutory interpretation. First, there is no express power in the UCA relating to oversight of competition or consideration of market outcomes - in fact, there is no mention of competition or market outcomes anywhere in the UCA.

12. Second, in terms of implied jurisdiction, it is self-evident that regulating public utility rates, service quality and reliability does not, as a "practical necessity", require the Commission to also regulate competition, or promote or avoid a particular market outcome in the TES market. As discussed below, it is also true that none of the factors cited by Corix and the Coalition -- i.e., (i) the UCA references to the public interest and the CPCN requirement, or (ii) British Columbia's energy objectives -- gives rise to implied jurisdiction to consider market outcomes in setting the CoC/TPP.

Jurisdiction Cannot Be Implied from CPCN Requirement or Public Interest Powers

13. Section 45 and other sections of the UCA referencing the public interest cannot be interpreted in the abstract, without consideration of the purpose of utility legislation. *Canadian Administrative Law* states as follows: "On the other hand, if a broad power must be

construed, a court should only include those powers that are rationally related to the purpose of the power."[10] [Emphasis in original.]

14. The Supreme Court of Canada made this clear in *ATCO,*[11] which addressed the interpretation of an ostensibly unlimited "public interest" power to set conditions on the sale of utility assets. The majority judgment stated:

> 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. [Emphasis added.]

The public interest powers in the UCA must be construed in light of the Commission's function as a regulator of public utility rates and service.

15. Corix cites the *BC Hydro* and *Shaw* cases[12] in highlighting the role of the CPCN in the context of utility regulation. It concludes based on those cases that:

> The Commission exercises regulatory control over important aspects of FEI's business and the use of its public utility resources, including:
>
> - The risks and costs that FEI may impose on the natural gas rate payers in support of the FAES AES business, and
>
> - The information, resources and market power that FEI may transfer from the natural gas business to the FAES alternative energy service business.

16. FEI takes no issue with the suggestion that the Commission may consider "costs and risks"; those considerations are fundamental to rate setting. However, Corix's first bullet misstates the implications of the relationship between FEI and FAES. There are no "additional risks and costs" being "imposed" on FEI customers. Rather, FEI is advocating a position that realizes *benefits* from economies of scope without additional risk to FEI customers. The

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[10] G. Gegimbald, *Canadian Administrative Law* (1st), p. 143.

[11] *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board),* 2006 SCC 4.

[12] Corix Submission, paras. 15-16.

customer groups intervening in this proceeding, which support FEI's proposal, appear to recognize this fact.

17. There is nothing in either of the *BC Hydro* or *Shaw* cases cited by Corix to support Corix's conclusion that the Commission exercises regulatory control over a public utility with respect to "market power that FEI may transfer from the natural gas business to the FAES alternate energy service business". To the contrary:

- The passage quoted by Corix from the *BC Hydro* case draws a direct link between the function of the CPCN and the Commission's role in setting rates, which is consistent with FEI's position. The regulatory compact arises from the grant of monopoly to the utility *via* a CPCN.[13]

- The *Shaw* case involved the interpretation of an express power in the UCA addressing sharing of utility infrastructure. There is no similar express power in the UCA relating to competition, nor is there any mention of competition or considering market outcomes. Given the existence of an express statutory power in respect of sharing of infrastructure, Corix is reading far too much in to the passage it has highlighted from *Shaw* ("I do not regard the relationship between utility and ratepayer and the function of rate setting as exclusively defining the scope of the regulatory arrangements.") in imputing jurisdiction to consider or promote specific market outcomes in competitive markets.

British Columbia's Energy Objectives

18. Corix cites "British Columbia's energy objectives", which must be considered in a CPCN application (but not in setting rates).[14] There is nothing in the definition of British

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[13] "Under the regulatory compact, the regulated utilities are given exclusive rights to sell their services within a specific area [i.e. a CPCN] 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." *ATCO*, para. 67. [Parenthetical added.]

[14] Corix Submission, para. 14.

Columbia's energy objectives that could be interpreted as conferring by "practical necessity" jurisdiction to consider market outcomes.

Contrast to Alberta

19. The absence of any reference to competition in the UCA stands in contrast to Alberta legislation. There is a different market structure in place in Alberta, and there are express provisions in the Alberta *Code of Conduct Regulation* dealing with "Preventing Unfair Competitive Advantage".[15] As COPE observed in its submissions, the BC legislature had determined that new legislation was required to confer a market oversight function on the Commission in the case of ICBC (the legislation was never proclaimed). The equivalent jurisdiction cannot simply be inferred in relation to BC public utilities from the existence of a CPCN requirement. A power to regulate competition or consider market outcomes is not, in the words of the Supreme Court of Canada, "a practical necessity for the regulatory body to accomplish the objects prescribed by the legislature".[16]

(b) The Commission Cannot Regulate Indirectly What it Cannot Regulate Directly

20. The Coalition urges the Commission to consider the interests of customers of third party TES providers. Corix avoids reference to competition and market outcomes, re-characterizing the issue as "inappropriate use of FEI resources"[17] or "the conduct of utilities in providing service".[18] Corix's and the Coalition's attempts to re-characterize their desired outcome contravenes the administrative law principle precluding the Commission from regulating indirectly what it cannot regulate directly.

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[15] Under section 108 of the Alberta *Electric Utilities Act*, the Minister make regulations "(g) establishing a code of conduct governing the relationship between (i) an owner of an electric distribution system and its regulated rate provider, (ii) an owner and its affiliated retailers, or (iii) the owner's regulated rate provider and an affiliated retailer, or any aspect of the activities of the parties in the relationship;". The *Code of Conduct Regulation* can be found at the following link. The provisions dealing with competition start at s. 19. http://www.qp.alberta.ca/1266.cfm?page=2003_160.cfm&leg_type=Regs&isbncln=9780779728824

[16] *ATCO*, para. 77.

[17] Corix Submission, para. 13.

[18] Corix Submission, para. 12.

21. The Coalition's focus on how the CoC/TPP will affect its competitive position is self-evident in its name (Coalition for Open Competition) alone. Although Corix has been more circumspect, it is not hard to see through Corix's attempt to re-characterize the issue. Its characterizations beg the critical question: why does Corix regard the use of FEI's resources as "inappropriate" or FEI's "conduct" as problematic? The obvious answer to this question, based on the sum total of Corix's submissions, is that Corix believes FEI resources should not be used in a manner that benefits FAES because conferring benefits on FAES might affect the TES market. This belief is particularly apparent where Corix later expresses concern about FEI transferring "market power" to FAES.[19] Regardless of how Corix might characterize its position, it is in substance advocating the same end result - consideration of market outcomes - that the Commission had correctly determined in the RMDM Decision (based on legal advice of Commission counsel) to be beyond its jurisdiction.

22. The Commission is not permitted to regulate indirectly (i.e., as an issue of "utility conduct" or otherwise) what it cannot regulate directly (i.e., regulate competition or consider market outcomes). The following passage from a 2010 decision of the Supreme Court of the Northwest Territories captures this established administrative law principle in the utility regulation context. The court in that case found that a Board order that had purported to address costs relating to the current test period was void because it, in substance, skirted the rule against retroactive ratemaking:

> [65] Any attempt to deal with the refunds received for 2007 within the context of the 2008-2010 rate application is, in my opinion, tantamount to retroactive ratemaking. Calling it a "prospective adjustment" is merely doing indirectly what cannot be done directly. It is axiomatic that the courts will look to the substance of what is being done, and not merely the form, and strike down any attempt to do indirectly what a tribunal's enabling statute does not allow to be done directly: see, for example, Reference re Agricultural Products Marketing Act, [1978] 2 S.C.R. 1198 (at p. 1291).
>
> [66] It may well be, as the Intervenors' counsel suggested, that the Board in this case, as opposed to what was done in the Alberta case, was trying to strike a better balance between the interests of consumers and those of the utilities. The difficulty is that in its attempt to do so the Board exceeded its jurisdiction by

[19] Corix Submission, para. 17.

engaging in what I previously described as both retroactive and retrospective ratemaking.[20]

23. The Commission must look past Corix's and the Coalition's characterization of the orders they are seeking, and look at their true intent and result - i.e., producing a particular market outcome favourable, or not disadvantageous, to Corix and the Coalition. That is not the role of the Commission.

(c) CoC and TPP Must Be Rooted in a Rate Setting Function

24. The Commission is exercising a rate setting function in establishing a CoC and TPP, not a broader public interest mandate. A key component of the Commission's rate setting mandate is to ensure that rates are not "more than a fair and reasonable charge for service of the nature and quality provided by the utility".[21] This phrase, which is found in the section of the UCA that defines "just and reasonable" rates, encompasses cost, service quality and reliability considerations. A direct link must exist between the provisions of a CoC/TPP and the Commission's mandate to ensure that rates are not "more than a fair and reasonable charge for service of the nature and quality provided by the utility". The CoC/TPP provisions must not go beyond what is required for that purpose.

25. FEI's proposals on the main areas of contention accomplish what is necessary to address impacts to ratepayers as captured in the phrase "just and reasonable":

- ***CoC Section 1: Transfer Pricing / TPP Generally:*** Appropriate transfer pricing rules ensure that the utility obtains fair value for labour and back office services provided to another affiliated entity. The ultimate objective is to ensure that the rates charged to utility ratepayers reflect the appropriate amount of revenue (in the case of FEI) or costs (in the case of the ARBNNM). As the purpose is not to level the playing field in the TES market, the pricing should be based on what is appropriate to capture economies of scope for FEI and the ARBNNM. It should not dis-incent the ARBNNM from using the services.

[20] *Northland Utilities (Yellowknife) Limited v. Northwest Territories Public Utilities Board*, 2010 NWTSC 92.
[21] UCA, s.59(5)(a).

- ***CoC Section 2: Shared services and personnel:*** Appropriate rules relating to shared services and personnel ensure that there is compensation flowing to FEI for the use of utility personnel. They also mitigate the risk that utility personnel will be used in a manner that is detrimental to the nature and quality of the service provided by FEI (i.e., personnel and market information used without compensation[22]). There is every reason to conclude that the provisions FEI has proposed are up to the task.

  The provisions addressing shared services and personnel cannot be developed giving consideration to factors relied upon by Corix and the Coalition, such as (i) the fact that the Coalition and Corix do not have access to services from FEI, (ii) a desire on the part of other TES providers to increase FAES' executive costs by precluding sharing, or (iii) the lingering suspicions of Corix and the Coalition that, notwithstanding the safeguards in place, FEI employees will act in bad faith or otherwise not follow the rules.

C. USE OF THE FORTISBC NAME

26. The Coalition has devoted several pages of its submission to its concern about FAES using the FortisBC name. The essence of the Coalition's submission is that "to appropriately protect consumers from confusion as to whether they are dealing with the natural gas utility or another FortisBC entity, the Commission should require the CoC to include a clarification statement."[23] FEI submits that the Commission should not accede to the Coalition's request for several reasons.

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[22] One of the concerns cited by the Coalition is the potential for commercial information to be imparted to FAES via shared executives. The Coalition portrays the disclosure of commercial information as inherently objectionable. In fact, the objectionable outcome is the disclosure of commercial information *without realizing its value in accordance with section 3 of the CoC.* Section 3 of the CoC, about which there is general stakeholder agreement, states in part: "Customer information will be provided at a reasonable price reflecting market circumstances and cover the cost of extracting and providing the information. All parties should pay the same price for the same or similar information." This requirement is thus also related to how much customers ultimately pay for service (i.e., just and reasonable rates) rather than market outcomes.

[23] Coalition Submission, para. 22.

27. First, in terms of any risk of confusion, FAES' use of "FortisBC" as a trade name is no different from Corix or Coalition members using their trade names to sell utility services when that trade name is also used by affiliates. Legal documentation always references the corporate entity with whom a customer is contracting. The use of a legal corporate name is sufficient notice to a customer or potential customer of the entity legally responsible for providing service.

28. Second, the Coalition has overlooked some important facts in crafting its three hypothetical scenarios that it claims might give rise to confusion[24]:

- There would have to be a Commission process for FAES or its projects to be sold. The scenario where a customer "suddenly becom[es] aware that he/she is no longer dealing with FortisBC"[25] could not occur.

- All customers of FEI, including those customers taking service from FAES as well, have the ability to refer to (i) their contract with FAES to determine the consequences of non-payment for thermal energy service, and (ii) FEI's published natural gas tariff to confirm their rights and obligations vis a vis FEI's natural gas service. Customers also have access to the Commission as a resource.

- The Coalition suggests that a potential customer of FAES would "mistakenly assume that they get some sort of discount or leverage in negotiation [with FAES] because they have linked their thermal energy service with its natural gas service". This hypothetical is not a practical concern. FEI is precluded from making such a claim by section 4 of the proposed CoC. FEI submits that it will also be in FAES' longer term interest to maintain its integrity and reputation. Developers contemplating TES projects are generally going to be reasonably sophisticated. Moreover, whatever perception a potential customer might

[24] Coalition Submission, para. 15.

[25] Coalition Submission, para. 14.

initially have about its leverage during negotiations, it will be in a position to compare FAES' offering to the offerings of other TES providers.

29. The Coalition asks the Commission to infer from the way in which the Delta School District has reported its financial information that the School District was confused about with whom it was dealing (FEI and FAES). The Coalition did not present any evidence on the School District's reporting practices. The inference that the Coalition seeks to draw in the absence of evidence also gives little credit to the relatively sophisticated nature of the customer.[26] The Commission cannot infer confusion from the evidence properly before it.

30. The Coalition, in support of its desired "clarification statement", draws an analogy to the Commission requiring Stream A system providers to notify customers that the Commission is not reviewing the rates and that the customers will have recourse to the Commission on a complaints basis.[27] The analogy is inapt. The Commission's clarification in the context of Stream A systems relates directly to the proper role of the Commission in overseeing rates and service quality. The clarification statement requested by the Coalition, by contrast, is aimed at a perceived deceptive market practice (or as the Coalition puts it, "to appropriately protect consumers from confusion"). The FortisBC name is being used appropriately. Moreover, there is a separate legal regime governing acceptable trade practices, just as there is for the regulation of competition. There is nothing in the UCA that empowers the Commission to oversee how any public utility brands itself.

31. In short, the Commission has correctly determined in the past that it has no jurisdiction to prevent entities from using the "FortisBC" brand[28], and the clarification statement sought by the Coalition would similarly amount to overseeing a utility's use of a licensed brand.

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[26] The Commission noted in the DSD Decision, at p.83 that "the Service Agreements were negotiated in good faith by two sophisticated parties".

[27] Coalition Submission, para. 21.

[28] The proposed CoC recognizes that FEI does not own the "FortisBC" brand in any event.

D. SIGNIFICANCE OF THE AES INQUIRY REPORT

32. The Coalition and Corix have suggested that FEI ought to have sought reconsideration and variance of elements of the AES Inquiry Report instead of proposing elements of the CoC/TPP that depart from the Report.[29] FEI addressed this argument in detail in its Pre-Hearing Conference Submissions[30] and in oral submissions at the Pre-Hearing Conference. This Application process was established at the Commission's direction in the AES Inquiry Report to address the CoC and TPP[31]. The Commission should be reviewing FEI's proposals on their merits.

[29] Coalition Submission, para. 40.

[30] Exhibit B-4, Response to Issue 5.

[31] AES Inquiry Report, Appendix H, p. 4.

PART THREE: SUBMISSIONS ON AREAS OF SUBSTANTIVE DISAGREEMENT

33. FEI addresses below the submissions of interveners on areas of substantive disagreement.[32] Corix and the Coalition are alone on the key issues of shared services and personnel and pricing rules.

A. CODE OF CONDUCT SECTION 2 - SHARED SERVICES AND PERSONNEL

34. FEI's proposal with respect to Shared Services and Personnel is set out on p.7 of the Application. It precludes the sharing of business development staff, but otherwise provides flexibility for resource sharing arrangements that (i) benefit both FEI customers and ARBNNM/FAES customers, and (ii) present limited potential for disclosure of confidential information outside what is permissible in section 3 of the CoC. Customer groups support FEI's proposal. The Coalition instead suggests that "the Commission require the elimination of 'dual roles' in the operations of FEI/FAES executives and that the Senior Executive in FAES report directly to the CEO of the holding company."[33] The Commission should reject the Coalition's suggestion.

35. The Coalition's position is premised on the Commission having jurisdiction to consider market outcomes. For instance, the Coalition's stated rationale for prohibiting shared executives is as follows:

> In the event that FAES receives timely, market information that is not available to all market participants, FAES will have an advantage in negotiating for potential TES projects. This has the possibility of making the TES market less competitive, thereby potentially raising TES rates to what would become an FAES customer.

The Commission should be focussed on ratepayers, without considering the market result of its determination. The only basis upon which the Commission could limit sharing of executives is if the limitation is necessary to protect FEI customers. A prohibition on sharing utility executives would increase costs for both utilities, particularly FAES. It would be inappropriate for the

[32] Exhibit B-4.

[33] Coalition Submission, para. 35.

Commission to take measures to the disadvantage of both utilities and their regulated ratepayers when the use of commercial information in the hands of FEI can be managed via the means proposed by FEI without additional costs being imposed.

36. The Coalition raises the prospect that FEI executives might one day obtain compensation from FAES when FAES is profitable, thus giving those executives an incentive to share market intelligence with FAES garnered in their role with FEI.[34] FEI submits that it would be inappropriate for the Commission to determine rules based on a presumption that utility executives of the future will deliberately act in contravention of their CoC obligations for monetary gain. The following comment from the *ATCO* decision is apt:

> 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.[35]

As the law is clear that regulators must presume good faith in the regulation of public utilities,[36] the Commission should not consider the Coalition's hypothetical scenario.

37. FEI's proposed CoC is consistent with the wording contained in FEI's existing CoC for Non-Regulated Businesses. It is also consistent with the Code of Conduct in place in Alberta, despite the additional market oversight jurisdiction conveyed by Alberta legislation that would have permitted the AUC to dictate a market outcome. It is a reasonable means of guarding against any confidential information being used contrary to what is permissible under CoC section 3, while permitting the two utilities to achieve legitimate economies of scope.

B. CODE OF CONDUCT SECTION 8 - FINANCING AND OTHER RISKS

38. The Coalition's opposition to FEI's proposal appears to be premised on an assumption that there is something inherently wrong with FEI providing financing to an

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[34] Coalition Submission, para. 33.

[35] ATCO, para. 84.

[36] This presumption is a key element of the well-established prudence test as articulated in the *Enbridge* decision and adopted by this Commission.

ARBNNM, even with prior approval of the Commission. For instance, the Coalition states "at some point in the future (10 years, 20 years, or longer) it will be cast as 'Yes, it is OK, we just need to apply' and there will be an assumption that this sort of financing was contemplated and is reasonable."[37] FEI submits that dogmatic opposition to a utility financing an ARBNNM is not justified based on ratepayer considerations alone. The Coalition is again basing its arguments on jurisdiction that does not exist. FEI's approach is supported by the Alberta Utilities Commission's CoC provisions discussed in FEI's Final Submissions.

39. BCOAPO's view is that "there does not appear to be any benefit to FEI ratepayers in allowing FEI to provide this assistance."[38] That might be true in many instances. However, there could also be circumstances where debt financing poses only modest risk to FEI customers, while also generating a benefit. The important point is that, under FEI's CoC proposal, the Commission will have the final say on the matter based on the specifics of any financing proposal. FEI is already subject to the Commission's ring-fencing order that precludes it from financing an affiliate, subject to further order of the Commission.[39] FEI's proposal, which is supported by the CEC[40] and not opposed by BCSEA-SCBC, aligns with the existing order.[41]

C. TRANSFER PRICING POLICY – SECTION 1 PRICING RULES, (ii) AND SECTION 2 DETERMINING COSTS

40. FEI responds below to the submissions of interveners on the TPP.

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[37] Coalition Submission, para. 26.

[38] BCOAPO Submission, para. 9.

[39] Order No. G-49-07, Reasons for Decision, p.1 of 15, Condition 7.2.1(3)(a): "No Terasen Utility will lend to, guarantee or financially support any affiliates of the Terasen Utilities, other than between TGI and TGS, or as otherwise accepted by the Commission."
http://www.fortisbc.com/About/RegulatoryAffairs/GasUtility/NatGasBCUCSubmissions/Documents/04-30_G-49-07_Reasons_for_Decision_Fortis_Acquisition.pdf

[40] CEC Submission, p.2.

[41] The Coalition has cited a 21 year old order relating to the 1993 reorganization of BC Gas (Coalition submission, para. 25). The 1993 Order addressed financing of NRBs only. The ring-fencing order currently in place for FEI as a result of the acquisition by Fortis Inc. applies to all FEI affiliates and makes it unnecessary for the Commission to consider the 1993 order.

(a) Response to Customer Submissions

41. The interveners representing the customers of FEI and FAES, all of whom stand to benefit from capturing economies of scope, generally support FEI's TPP proposal and oppose the proposals of FAES' competitors.

42. At one point in its submission, BCOAPO adds a proviso: "provided that in all cases an incremental benefit can be shown to accrue to FEI ratepayers. If no benefit accrues to FEI ratepayers from a transaction, FEI should not be permitted to undertake the transaction."[42] It is not clear whether BCOAPO is asking for case by case review of every cost, but in any event review of that nature would be impractical and unnecessary. The facts that (i) FEI employees are providing services to FAES over and above the role they play for FEI, (ii) FEI's charge out rates reflect the market for labour (either through collective bargaining or establishing management compensation to be competitive with market rates), and (iii) there are recoveries of fixed overhead costs like facilities charges and general overhead loading[43], are sufficient demonstration of the benefits to FEI customers. No further vetting is required on a case by case basis, if that is indeed what BCOAPO was suggesting.

(b) Response to Coalition's Submissions

43. The Coalition's submissions on the TPP are, once again, focussed on market regulation and not on achieving just and reasonable rates. Its primary point is that "Non-FAES thermal energy service providers have no access to FEI's experienced and knowledgeable staff".[44] The Coalition maintains that the expertise and familiarity of the FEI staff with FAES requirements thus "raises the question as to what 'premium' should be applied to the transfer price of services from FEI to FAES in light of the enhanced access to premium resources."[45] The Coalition is seeking a remedy that falls beyond the Commission's jurisdiction. It is not open to the Commission to impose a premium on the transfer price charged by FEI in order to nullify

[42] BCOAPO Submission, para. 12.

[43] BCUC IR 6.1 and 6.2.

[44] Coalition Submissions, para. 37.

[45] Coalition Submissions, para. 37.

the benefit FAES might obtain relative to its competitors from having access to knowledgeable FEI staff.

44. The Coalition suggests that FEI's proposal incents FEI to create surplus capacity. A full answer to this argument is that the Commission oversees FEI's revenue requirements. Under cost of service regulation, the Commission examines the departmental costs (including FTEs) and the utility has an incentive to reduce costs within each test period. FEI has an even stronger incentive under PBR to avoid surplus capacity because reducing FTEs will increase FEI's earnings (other things being equal) for the duration of the PBR term. Customer groups involved in this proceeding implicitly recognize that the potential to achieve economies of scope will necessarily exist even though FEI's operations are managed efficiently.

(c) Response to Corix's Submissions

45. Corix asserts at paragraphs 25 and 27 that FEI's cost allocation methodology "captures only part of the true cost of serving the FAES AES business. Natural gas ratepayers absorb all other costs and risks and, therefore, the general promotion of the FEI AES business." It goes on to claim as follows:

> Since transfer costs to FAES only start when a project proceeds, the cost associated with efforts to develop AES projects (some of which may never proceed) are borne by the FEI ratepayers in the interim. The shareholders of FEI are shielded from financial risk and FAES receives a business development subsidy at the expense of the natural gas ratepayers.

Corix is mistaken as to the evidence:

- Corix is starting from a flawed premise that "transfer costs to FAES only start when a project proceeds". Costs of business development are incurred by FAES employees, not FEI; FAES has its own business development staff.[46] Back office support by FEI is charged to the Thermal Energy Services Deferral Account (TESDA), irrespective of when the work is done.[47]

[46] FEI Supplemental Information, Response to Question 2, p.4.

[47] See FEI Reply Submission, para. 6.

- All TES related costs, whether incurred by FEI or by FAES, are recorded in the TESDA.[48] The TESDA has always been segregated from the natural gas class of service rate base. FEI customers are not at risk for the balance in the TESDA.

- Because the TESDA is kept separate from the natural gas rate base, financing costs for the TESDA balance are also captured in the TESDA. They are not borne by FEI's natural gas customers.

- Costs captured in the TESDA, including business development costs are transferred to FAES projects. The entire remaining balance in the TESDA is being transferred to FAES by January 1, 2015. Any costs that FAES cannot recover from TES customers will, by default, be borne by FAES' shareholder.

- There is clear language in sections 3.2 and 3.3 of the proposed TPP regarding research and development costs to reinforce that FEI customers are not paying for such costs related to FAES.

46. Corix states in paragraph 31 that its preferred pricing formulation "allows FEI ratepayers to realize the full value for the transferred service or asset rather than just a limited contribution to cost." As other customer interveners have observed, increasing the price FEI charges to FAES to the higher of market price or fully allocated cost only drives the ARBNNM to obtain the service from elsewhere and does not increase the benefit to FEI ratepayers. It is worth repeating that when FEI staff carry out their responsibilities, natural gas customers receive priority of service and FAES' requirements are in secondary priority; that would not be the case with third party providers, which adds to the value proposition of third party providers relative to FEI. FAES has been investigating alternatives to replace some of the services currently provided by FEI.[49]

47. Corix argues at paragraphs 32 and 33: "If the 'some contribution is better than none' logic is applied fully, then FEI should offer its discounted service and assets to all AES

[48] BCUC IR 1.6.8.

[49] BCUC IR 1.6.3; COPE IR 1.3.

providers." Corix suggests that FEI's unwillingness to provide services to the TES market generally is evidence that it is promoting FAES' business. Corix's argument ignores the fact that FEI is not in the business of selling labour and back office services. Capturing economies of scope by providing service to an affiliate is simply good management. FEI need not add any incremental staff to achieve this objective. Selling labour and back office services to a broader market for those services would be a fundamentally different business model with its own risk profile.

(d) Summary

48. In summary, the Commission should be setting CoC/TPP provisions that ensure that FEI, FAES and their respective customers, are treated fairly. Each of these stakeholders is treated fairly by FEI's proposal.

PART FOUR: APPROPRIATE SAFEGUARDS IN PLACE

49. The Coalition and Corix have made submissions on the nature of the safeguards in place to support the objectives of the Coc and TPP. FEI addresses their main submissions below. FEI submits that its proposed mechanisms are appropriate and should provide the necessary comfort to the Commission that FEI will give effect to the intention of the CoC and TPP.

A. COMPLAINTS PROCESS

50. The Coalition maintains that any complaints should be received by the Commission directly, rather than referred to FEI in the first instance.[50] FEI's proposal reflects what has long been in place in the existing CoC for NRBs. There is no compelling reason to depart from it.

B. TIMEKEEPING

51. The Coalition expresses a preference for changing FEI's existing practice of exception-based timekeeping so that "all FEI employees that provide services to FAES account for 100% of their time, not just the portion that is attributed to FAES."[51] Corix makes a similar argument, going so far as to suggest that the result of FEI's existing practice "is that the FEI ratepayers bear the greater burden of carrying the staffing cost for the combined business."[52]

52. Employees are still accounting for 100% of their time through exception-based reporting. FEI submits that the approach advocated by the Coalition and Corix is contrary to the best interest of FEI and its customers. Neither the Coalition, nor Corix has identified any evidence or logical reason why changing FEI's timekeeping practices in the manner they have proposed would:

- improve the accuracy of timekeeping,

[50] Coalition Submission, para. 41.
[51] Coalition Submission, para. 45.
[52] Corix Submission, para. 25.

- be more transparent, or
- result in more costs being allocated to FAES.

FEI submits that its current approach is no more or less accurate or transparent than the approach the Coalition and Corix advocate. Changing the existing approach would, however, potentially introduce administrative inefficiency for the purpose of accounting for what is, in reality, a very small amount of time relative to the total work time of FEI employees. FEI has allocated costs based on its existing approach for a number of years in a variety of contexts beyond just allocating time to FAES. FEI has introduced additional oversight by the Director of Finance to review charges on a quarterly basis and require confirmation from department managers, as discussed in FEI's Final Argument under "Safeguards Related to Transfer Pricing". The Commission should affirm FEI's proposed process.

PART FIVE: CONCLUSION

53. FEI's proposed CoC and TPP promote just and reasonable rates for FEI (the provider of labour and back office services) and FAES (the recipient of those services). FEI respectfully submits that the Commission should act in the interests of both affiliated utilities and their respective customers by approving FEI's CoC and TPP as proposed.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.

Dated: December 9, 2014

[original signed by Matthew Ghikas]
Matthew Ghikas
Counsel for FortisBC Energy Inc.

BOOK OF AUTHORITIES

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CANADIAN ADMINISTRATIVE LAW

FIRST EDITION

Guy Régimbald

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right he has jurisdiction to go wrong. Neither an error in fact nor an error in law will destroy his jurisdiction.[5]

Put simply, jurisdiction means authority or power to decide. Historically, if an administrative tribunal was empowered to make a decision on a question of law or fact, its ultimate decision could not be reviewed judicially or reversed on appeal: If a tribunal had jurisdiction to entertain the question, it could not subsequently lose its jurisdiction by coming to a wrong conclusion, whether in law or in fact,[6] even if its decision was entirely without evidence.[7] Thus, if the decision maker properly determined, at the outset, that it had the power to decide, its ultimate decision was shielded from judicial review. The nature of the administrative decision maker's jurisdiction is determinable "at the commencement, not at the conclusion, of the inquiry".[8] If an administrative decision maker had made an error as to its powers or the scope of its authority, its decision was illegal, and thus quashed because it was *ultra vires*. Consequently, once it was established that the tribunal had jurisdiction at the outset of the inquiry, the decision was final and conclusive. This gave rise to the concept of the "right to err" in administrative law. This error was only possible "within jurisdiction" or, in other words, only after the decision maker had first properly construed the extent of its authority.

Nevertheless, courts still found ways to intervene in particularly outrageous decisions by devising the concept of "error on the face of the record", which allowed courts to intervene and inquire into the substance or the merits of the administrative decision. This has later been confirmed and transformed into the doctrine of "reasonableness" or "rationality". The rationale for this fundamental change was that the administrative decision maker, even if it had *prima facie* jurisdiction to make a decision, had to retain it unimpaired until it had discharged its task.[9]

2. FUNDAMENTAL CONCEPTS

Administrative decision makers are creatures of statute. They cannot exceed the powers that were granted to them by their constituting statute

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5 See H.W.R. Wade & C.F. Forsyth, Administrative Law, 9th ed. (New York: Oxford University Press, 2004) at 262.

6 *R. v. Central Criminal Court JJ.* (1886) 17 QBD 598 at 602.

7 *R. v. Shropshire JJ., ex p. Blewitt* (1866) 14 L.T. 598; *Ex p. Hopwood* (1850) 15 Q.B. 121.

8 *R. v. Bolton* (1841) 1 Q.B. 66, 74.

9 H.W.R. Wade & C.F. Forsyth, *Administrative Law*, 9th ed. (New York: Oxford University Press, 2004) at 263.

and must remain within the confines of their jurisdiction or authority.[10] Professor Paul P. Craig, in his text *Administrative Law*,[11] illustrated the true nature of delegation of powers, or "jurisdiction", with a formula:

> All grants of authority may be expressed in the following manner: if X exists the tribunal may or shall do Y. X may consist of a number of different elements, factual, legal and discretionary.[12]

Thus, for a decision maker to have jurisdiction, it must have correctly interpreted all of the "X" elements, the conditions precedent to the exercise of jurisdiction. If it makes an error in the construction of any of those, a court, on judicial review, may intervene by exercising its inherent powers to interpret the intention of Parliament. If it was not Parliament's intention to delegate the authority to decide to that specific body, then its decision on the merits, no matter how reasonable, is *ultra vires*.

2.1 PRINCIPLES OF INTERPRETATION OF JURISDICTION

In order to determine whether the power was indeed granted by the legislature to the administrative decision maker, the Supreme Court has indicated that the normal principles of statutory interpretation apply:

> 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.
>
> [...]
>
> 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.[13]

In administrative law, two sources need to be examined in determining the specific contours of an administrative decision maker's jurisdic-

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[10] *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] S.C.J. No. 4 at para. 35, [2006] 1 S.C.R. 140 (S.C.C.).

[11] Paul P. Craig, *Administrative Law*, 5th ed. (London: Sweet & Maxwell, 2003) at 475.

[12] Paul P. Craig, *Administrative Law*, 5th ed. (London: Sweet & Maxwell, 2003) at 475.

[13] *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] S.C.J. No. 4 at paras. 36-37, [2006] 1 S.C.R. 140 (S.C.C.).

tion. Those two sources are: (1) an express grant of jurisdiction or power by the enabling statute; and (2) an implicit power necessary for the decision maker to be able to fulfil its mandate — the common law, under the doctrine of jurisdiction by necessary implication will fill any gap left by the legislature.[14]

The normal principles of statutory interpretation will apply to both sources of jurisdiction. First, a court must consider the grammatical and ordinary meaning of the words used in determining the powers granted by the enabling statute. Second, if the enabling statute is silent on a specific power, or the scope of the authority or jurisdiction of the decision maker remains elusive, the court will look at the context. As held by the Court:

> [G]rammatical 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.
>
> [...]
>
> 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.
>
> [...]
>
> 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.
>
> 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). Cana-

[14] *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] S.C.J. No. 4 at para. 38, [2006] 1 S.C.R. 140 (S.C.C.).

> dian 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.[15] (emphasis added)

Consequently, in determining the scope of the jurisdiction of a decision maker, a reviewing court should always use the basic principles of statutory interpretation. The exercise is no different than in other legal contexts; the objective is to divine the intent of the legislature. This being said, when jurisdiction is expressly conferred, the inquiry may be fairly simple.

However, where the doctrine of jurisdiction by necessary implication is needed, because the authority is implicitly conferred to the decision maker, statutory interpretation will be of less help in the case where the court must include a broad power within the jurisdiction of the decision maker, as opposed to a narrowly drawn one. Purposive analysis allows a court to include any "narrow" powers, by necessary implication, to allow the decision maker to achieve its purpose. On the other hand, if a broad power must be construed, a court should only include those powers that are rationally related to the purpose of the power.[16]

The rationale is the same for both types of jurisdiction by necessary implication. A specific "narrow" power may be needed by necessary implication to enable the decision maker to fulfil its mandate. In other cases, a court will have to construe a "broad power" to enable the same, and it may do so if the decision maker would be paralysed otherwise. This type of interpretation is necessary because it is always presumed that the legislature did not intend to enact legislation that would be lead to absurd consequences.[17] But for the inclusion of a power by necessary implication, the intent of the legislature would be negated.

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15 *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] S.C.J. No. 4 at paras. 48-51, [2006] 1 S.C.R. 140 (S.C.C.).

16 *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*, [2006] S.C.J. No. 4 at para. 74, [2006] 1 S.C.R. 140 (S.C.C.); see Ruth Sullivan, *Sullivan and Driedger on the Construction of Statutes*, 4th ed. (Markham, Ont.: Butterworths, 2002) at 228.

17 *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] S.C.J. No. 2 at para. 27, [1998] 1 S.C.R. 27 (S.C.C.).

2.2 JURISDICTIONAL ERROR

2.2.1 *ULTRA VIRES*

The principle that a public authority may not act outside its powers (or act *ultra vires*) might appropriately be considered to be the central principle of administrative law.[18] Statutory bodies to which specific powers are delegated may only deal with matters over which they have authority, and may not abuse that authority. They must always demonstrate that their actions are within "the four corners of their jurisdiction",[19] and fall squarely within the boundaries set by legislation. If a court determines that a public body or decision maker acted outside the powers allocated to it, its actions will be declared void because they are *ultra vires*. In essence, the doctrine of *ultra vires* allows courts to strike down administrative decisions made by bodies exercising public functions for which the body has no power. Acting *ultra vires* and acting without jurisdiction have essentially the same meaning.[20]

If a public authority makes an order which it has no authority to grant, the order will be illegal and of no use. Since the decision has no legal leg to stand on, it is a nullity. This conclusion applies to both types of jurisdictional errors discussed above, whether the decision maker never had the authority to even inquire on the issue, or if the decision maker subsequently lost jurisdiction by ordering a remedy that it could not order or by making an unreasonable error.

The doctrine of *ultra vires* has been given a very wide meaning. Courts have also extended the meaning to limit the powers of Parliament. Given that Parliament is sovereign, it may delegate any decision to a public body. Since courts may not interfere with an action within the competence of the decision maker as authorized by Parliament, courts have had to resort to implied limitations to the delegated authority. The doctrine of *ultra vires* has permitted courts to intervene in errors within the jurisdiction of the decision maker. By interpreting an implicit duty of fairness, for example, into the decision making process, courts have been able, through the use of the doctrine, to strike abusive decisions when they are, at first glance, legal.

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18 Approved in *Boddington v. British Transport Police*, [1998] H.L.J. No. 13, [1999] 2 A.C. 143 at 171 (H.L., Lord Steyn); H.W.R. Wade & C.F. Forsyth, *Administrative Law*, 9th ed. (New York: Oxford University Press, 2004) at 35.

19 As characterized by Paul P. Craig, *Administrative Law*, 5th ed. (London: Sweet & Maxwell, 2003) at 475.

20 S.A. De Smith H. Woolf & J.L. Jowell, *Principles of Judicial Review*, 5th ed. (London: Sweet & Maxwell, 1995) at 95.

Because courts can stretch the meaning of the doctrine to mean almost anything by finding limitations in Parliament's grant of jurisdiction, the doctrine has become somewhat artificial in its application. The malleability of the *ultra vires* doctrine has led Sir John Laws to the conclusion that the principle is merely a tautology, in the following sense: Because the principle does not itself indicate what is to count as a want of power, invocation of the principle amounts to saying no more than that the court will strike down what it chooses to strike down.[21]

2.2.2 PRELIMINARY OR COLLATERAL QUESTION DOCTRINE

The concept of jurisdiction has also given rise to the "preliminary", "collateral" or "jurisdictional" question. The collateral or preliminary question is one that any decision maker must pose to itself before embarking on any inquiry, and answer correctly. In essence, the question is: Was it Parliament's intent to delegate that decision-making to that specific decision maker? The question is thus not "the actual matter committed to its decision",[22] upon which the tribunal's own decision is conclusive.[23] A preliminary or collateral question is said to be one that is collateral to "the merits"[24] or to "the very essence of the inquiry".[25] Put simply, as argued by Professor Craig, a preliminary or collateral question is nothing more than determining the "four corners" of a tribunal's jurisdiction, or the interpretation of the X factors. Thus, prior to undertaking the analysis of the merits and considering the facts, an administrative decision maker must first correctly determine the extent of its authority to make the ultimate decision. On review, a court of inherent jurisdiction would also have to review the correctness of that particular assessment. If that was not the case, the administrative body would have the sole discretion to determine the powers vested in it and could "wield an absolutely despotic power, which the legislature never intended that it should exercise."[26] Consequently, while the administrative decision maker is

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21 Paul P. Craig, *Administrative Law*, 5th ed. (London: Sweet & Maxwell, 2003) at 14-15; J. Laws, "Illegality: The Problem of Jurisdiction", in M. Supperstone and J. Goudie (eds.), *Judicial Review*, (Butterworths, 2nd ed., 1997) at 3.

22 *R. v. Lincolnshire Justices ex p. Brett*, [1926] 2 K.B. 192 at 202 (Eng. C.A.), *per* Atkin L.J.

23 See H.W.R. Wade & C.F. Forsyth, *Administrative Law*, 9th ed. (New York: Oxford University Press, 2004) at 255.

24 *Bunbury v. Fuller* (1853) 9 Ex. 111, 140.

25 *Ex p. Vaughan* (1866) L.R. 2 Q.B. 114 at 116.

26 *R. v. Marsham*, [1892] 1 Q.B. 371 at 379.

Date: 2010 11 24
Docket: S-1-CV-2010000079

IN THE SUPREME COURT OF THE NORTHWEST TERRITORIES

BETWEEN:

NORTHLAND UTILITIES (YELLOWKNIFE) LIMITED and
NORTHLAND UTILITIES (NWT) LIMITED

Applicants

- and -

NORTHWEST TERRITORIES PUBLIC UTILITIES BOARD

Respondent

- and -

CITY OF YELLOWKNIFE and
TOWN OF HAY RIVER

Intervenors

Application for leave to appeal and appeal of a decision by the Public Utilities Board.

Heard at Yellowknife, NT, on November 2, 2010.

Reasons filed: November 24, 2010.

REASONS FOR JUDGMENT OF THE HONOURABLE JUSTICE J.Z. VERTES

Counsel for the Applicant: Loyola G. Keough

Counsel for the Respondent: John Donihee

Counsel for the Intervenors: Thomas D. Marriott

Date: 2010 11 24
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IN THE SUPREME COURT OF THE NORTHWEST TERRITORIES

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- and -

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Intervenors

REASONS FOR JUDGMENT

[1] This is an application for leave to appeal and an appeal of a decision, numbered 4-2010, issued by the Northwest Territories Public Utilities Board (the "Board") on March 24, 2010.

[2] At the hearing before me, I granted leave and said that reasons for that decision would be forthcoming. Those reasons are contained within this judgment. Since counsel at the hearing were ready and willing to also argue the appeal on the merits, I proceeded to hear that as well. This judgment therefore also contains my reasons for decision on the appeal.

[3] The issue put before the court is whether the Board exceeded its jurisdiction when, as part of its ratesetting exercise for the period 2008-2010, it ordered the

applicants to flow through to customers money received as a result of a tax refund for operations in 2007. The Applicants say it did and that its order amounts to retroactive ratesetting. The Intervenors argue that it is prospective ratesetting since it seeks to redress harm to current customers. The Board takes no position. For the reasons that follow, the appeal is allowed.

Background:

[4] The Board is established by the *Public Utilities Act*, R.S.N.W.T. 1988, c.24 (Supp.), to regulate public utilities in the Northwest Territories. It has jurisdiction to supervise the operations of utility companies, to approve municipal franchise agreements, and, most significantly for purposes of this appeal, to fix rates for utility services. It is part of what has been described by the Supreme Court of Canada, in *ATCO Gas & Pipelines Ltd.* v. *Alberta (Energy & Utilities Board)*, [2006] 1 S.C.R. 140, as a "regulatory compact" (at para. 63):

> 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 ...(citations omitted)

[5] With respect to ratesetting, the Board regulates on the basis of specific years (called "test years"). It sets the rates for specific test years and once those rates are set they are final. The only exceptions to that are if the Board's order is merely an interim one or if a deferral account is established. Neither situation applies in this case.

[6] The Act contemplates that the objective for the Board is to fix "just and reasonable" rates. That is not explicit but in several sections dealing with ratesetting, such as subsections 49(1), 51(2), 51(3) and 51(4), the Act repeats the phrase "in fixing just and reasonable rates". In doing so, the Board determines a rate base consisting of the cost of the utility's property used to provide the service and its necessary working capital and then fixes a fair return on that rate base. All parties agree that the Act requires the Board to set rates on a prospective basis, such as described in *Northwestern Utilities Limited et al* v. *The City of Edmonton*, [1979] 1 S.C.R. 684 (at p. 691): "The statutory pattern is founded upon the concept of the establishment of

rates *in futuro* for the recovery of the total forecast revenue requirement of the utility as determined by the Board."

[7] All parties also agree on another basic tenet of ratesetting by public utility boards, that being that, in the absence of specific legislative authority to do so, boards do not have the authority to retroactively change rates: see *ATCO Gas & Pipelines (supra)*, at para. 71. Rates are raised or lowered to reflect current conditions. They are not designed to pay back past excessive profits or recoup past operating losses. The Board can take into account past experience in setting the current rates; but, it cannot design a future rate so as to enable the utility to recover a past loss or to rectify for customers some past over-compensation of the utility. In either case the Board would be engaged in retroactive or retrospective ratesetting.

[8] This case concerns one particular aspect of the utilities' overall finances, the treatment of stock handling charges. In February, 2008, both Applicants filed their respective rate applications for the test years 2008-2010. Up to that time, stock handling charges had been capitalized as part of the company's rate base and the capitalized amount added to the pool of capital cost allowances. As the review of their rate applications went on, the Applicants became aware that these stock handling charges could be claimed as tax deductions. This was because of a ruling from the Canadian Revenue Agency received by their parent company in Alberta. The Applicants decided in early 2008 to claim these deductions on their 2007 tax returns. The Applicants then amended their 2008-2010 rate filings to include the projected benefit of similar deductions in the test years.

[9] It is worthwhile to note that there was no rate application or ruling by the Board for 2007. Rates had been set for the period of 2005-2006 and these were used as the basis for the rates charged in 2007. So the 2008-2010 application was the first opportunity to review the impact of deducting these charges as opposed to capitalizing them.

[10] The amounts received back by the Applicants, as a result of taking these deductions, were relatively small. They were $19,400 for one and $3,800 for the other.

[11] On October 27, 2008, the Board issued two decisions, Decision 24-2008 and Decision 25-2008, dealing with the Applicants' 2008-2010 rate applications. Both decisions addressed the income tax deductions for stock handling charges in the same way:

> The Board notes NUL's treatment of stock handling charges for income tax purposes was different prior to the current test period. Prior to the current test period stock handling charges were not deducted for calculation of the income tax component of revenue requirement, both in the forecasts and in the actuals. As long as NUL's treatment of stock handling charges remains consistent for the forecasts as well as actuals, the Board considers customers will not be harmed. However, if NUL were to choose to follow the route of ATCO Gas and request that its prior year income taxes be reassessed by CRA to the maximum extent possible including deduction for stock handling charges then customers will be harmed if such charges were not were not flowed through to customers.

[12] Both decisions also contained a direction to the applicants that any tax refunds received as a result of claiming these deductions are to be "flowed through" to their customers. The Board's directions were as follows:

> In view of the foregoing, the Board will not direct NUL to retroactively adjust its deductions for stock handling charges respecting prior years. However, if NUL were to choose to request such deductions from CRA respecting prior years, the Board expects that any resulting income tax savings will be flowed through to NUL's customers.

[13] The Board did not say how the refunds are to be "flowed through" to the customers. But, both the Applicants and Intervenors assume that this means that the money received by the Applicants is to be paid over to the current customers.

[14] In January, 2009, the Applicants filed applications with the Board seeking a review and variance of these directions. The Applicants submitted that the stock handling charges related to a prior year, 2007, for which rates had been finalized, while the directions were contained within the Board's decisions relating to 2008-2010 rates. As such, so the Applicants argued, the Board's directions breached the principle against retroactive ratesetting and thus were outside the Board's jurisdiction.

[15] In March, 2009, the Applicants requested the Board to defer consideration of their review and variance applications pending the outcome of an identical dispute before the Alberta Utilities Commission. The Board agreed to do so

[16] On November 12, 2009, the Alberta Utilities Commission issued Decision 2009-215 respecting the treatment of tax refunds received by ATCO Electric Ltd. for similar deductions claimed for prior years. The reasons of the Commission will be discussed in further detail later in these reasons but, in summary, the Commission considered itself to be bound by the principle against retroactive ratemaking, the principle of prospectivity, and the principle of regulatory certainty, and therefore precluded from directing ATCO Electric, either directly or indirectly, to return these funds from prior years to current customers. I was told that this decision has not been appealed or judicially reviewed.

[17] The Board reviewed the Alberta decision and continued with consideration of the review and variance applications. On March 24, 2010, the Board issued Decision 4-2010 in which it dismissed the Applicants' request to vary its earlier directions. This is the subject-matter of this appeal.

Decision 4-2010:

[18] In its decision, the Board started by noting that the rates established for the 2005-2006 period, being the rates that were in place in 2007, were based on the assumption that stock handling charges cannot be deducted for tax purposes. Rather, those charges were capitalized as part of the companies' rate base and the capitalized amount added to the pool of capital cost allowances. It also noted that the Applicants, after they became aware of the deductibility of these charges, had the discretion as to whether to claim the stock handling charges as a deduction for 2007 and prior years but chose to claim only for 2007.

[19] These two points led to what I think are the main arguments supporting the Board's decision.

[20] First, the Board stated that there are certain methodological underpinnings to the establishment of rates. Two of those relate to the calculation of income taxes and capital cost allowance deductions. Any retroactive change in the methodology used in

the establishment of rates, without regard to its impact on future rates, is, in the Board's view, a violation of the principle of prospectivity. In dismissing the Applicants' argument that the Board's directions amount to retroactive ratemaking, the Board wrote:

> The Board considers the amount of Capital Cost Allowance (CCA) that is claimed as a deduction in one time period versus another, for tax purposes, is a timing issue. If more CCA is claimed in a past year, then less Un-depreciated Capital Costs pools would be available for use in future years resulting in a reduction in the CCA deductions in future years. Since CCA claims in a past year impact future year tax calculations, the Board considers any potential adjustments to future customer rates to reflect the carry over effects of past deductions to be not a retroactive adjustment of historical rates but rather a prospective adjustment to restore the integrity of prospective rate making.

[21] Second, the Board was persuaded by the argument advanced by the Intervenors in this case that, since the claiming of stock handling charges as a deduction is solely within the discretion of the Applicants, there is no shared risk as between the utilities and the customers. In other words, this is a purely one-sided benefit. It is not an "efficiency" saving but merely a windfall due to a fortuitous tax ruling and, because claiming higher deductions in one year has an impact on the amount of tax due in future years because of the reduction in capital cost allowance available, the risk results in harm to the customers.

[22] Therefore, the Board was not convinced that its earlier directions were either inconsistent with prospective ratemaking or violated the principle prohibiting retroactive ratemaking.

Application for Leave to Appeal:

[23] Section 78(1) of the *Public Utilities Act* restricts appeals to questions of law or jurisdiction and an appellant must first obtain leave to appeal.

[24] The parties agree on the test to be applied to determine whether leave should be granted: *North West Co.* v. *Town of Fort Smith*, [2007] N.W.T.J. No. 6 (S.C.), at para. 16; *Atco Electric Ltd.* v. *Alberta (Energy and Utilities Board)*, [2003] A.J. No. 117 (C.A.), at para. 17. The Applicants must demonstrate that the appeal raises a serious

arguable point. Subsumed within this test are four criteria: (1) whether the point on appeal is of significance to the practice; (2) whether the point raised is of significance to the action; (3) whether the appeal is *prima facie* meritorious; and, (4) whether the appeal will unduly hinder the progress of the case. Also taken into consideration is the standard of review that will apply should leave be granted.

[25] In my view, as I will explain more fully later, the appeal raises a question of jurisdiction. Assuming that the Board had the power to embark on an examination of how, if any, these tax deductions and refunds were to be treated, the issue is whether the Board exceeded its jurisdiction by imposing directions that were tantamount to retroactive ratemaking. And, if it is a jurisdictional issue, then the Board must be correct in law. Thus the issue is significant to the practice.

[26] The issue is obviously significant to the action since it is determinative of the action. So determination of this point will not hinder progress of the action.

[27] The Intervenors argued that the appeal is insignificant since the practical effect of the Board's directions are immaterial. By that they mean that the amount of dollars at stake amount to an insignificant part of the Applicants' total revenue requirements. But, of course, the Applicants respond that it is the principle that counts, not the dollars. This appeal is essentially about the jurisdiction of the Board in exercising its ratesetting powers.

[28] I agree with the points made by the Applicants. Hence, I granted leave to appeal.

Standard of Review:

[29] It is trite law to state that a tribunal has only those powers that are expressly or implicitly conferred on it by its constituent statute. Either the Board had the jurisdiction to issue the directions, or it did not.

[30] The first issue that must be addressed, therefore, is the standard of review. However, as stated in *Dunsmuir* v. *New Brunswick*, [2008] 1 S.C.R. 190, it is not necessary to perform an analysis of this issue if the standard of review for the type of question in issue has already been determined by the jurisprudence.

[31] Questions of jurisdiction are reviewed on a standard of "correctness": *ATCO Gas & Pipelines (supra)*, at para. 21. As previously mentioned, s.78(1) of the Act limits appeals to questions of law or jurisdiction. This generally calls for the application of the correctness standard: *Prairie North Regional Health Authority* v. *Kutzner*, [2010] S.J. No. 650 (C.A.), para. 31.

[32] Section 17 of the Act, however, states that the Board has exclusive jurisdiction for all matters in which jurisdiction is conferred on it by the Act and its decisions shall not be questioned or reviewed by judicial review or any other process. Section 19 provides that the Board's determination on a question of fact is conclusive and binding. These constitute privative provisions and therefore any question of fact is not subject to appeal.

[33] The Intervenors argued that the applicable standard of review is reasonableness since the issue, the direction to "flow through" to customers the benefits associated with any income tax reassessments, is one that calls for the special expertise enjoyed by the Board.

[34] There is no doubt that the Board is a specialized tribunal. But, in this case, the question is whether the Board exceeded its jurisdiction. If, as in the case of *Calgary* v. *Alberta (Energy and Utilities Board)*, [2010] A.J. No. 449 (C.A.), a case relied on by the Intervenors, the Board's jurisdiction is decided in its favour, then a review of its decision would be on the standard of reasonableness. But here the fundamental question is jurisdictional. Therefore correctness is the standard.

[35] When I speak of jurisdiction I am cognizant of the Supreme Court's admonishment that only "true" questions of jurisdiction attract the correctness standard of review. This was emphasized by Bastarache and Lebel J.J., writing for the majority, in *Dunsmuir (supra)*, at para. 59:

> Administrative bodies must also be correct in their determinations of true questions of jurisdiction or *vires*. We mention true questions of *vires* to distance ourselves from the extended definitions adopted before *CUPE*. It is important here to take a robust view of jurisdiction. We neither wish nor intend to return to the jurisdiction/preliminary question doctrine that plagued the jurisprudence in this area for many years. *"Jurisdiction" is intended in the narrow sense of whether or not the*

> *tribunal had the authority to make the inquiry. In other words, true jurisdiction questions arise where the tribunal must explicitly determine whether its statutory grant of power gives it the authority to decide a particular matter.* The tribunal must interpret the grant of authority correctly or its action will be found to be *ultra vires* or to constitute a wrongful decline of jurisdiction. An example may be found in *United Taxi Drivers' Fellowship of Southern Alberta* v. *Calgary (City)*, [2004] 1 S.C.R. 485. In that case, the issue was whether the City of Calgary was authorized under the relevant municipal acts to enact bylaws limiting the number of taxi plate licences. That case involved the decision-making powers of a municipality and exemplifies a true question of jurisdiction or *vires*. These questions will be narrow. We reiterate the caution of Dickson J. in CUPE that reviewing judges must not brand as jurisdictional issues that are doubtfully so. [Emphasis added; citations omitted.]

[36] The distinction between the "narrow" and "wide" meanings of jurisdiction was explained by Professors Jones and de Villars in their text, *Principles of Administrative Law* (5th ed.), at p. 140:

> In its broadest sense, "jurisdiction" means the authority to do every aspect of an *intra vires* action. In a narrower sense, however, "jurisdiction" means the power to commence or embark on a particular type of activity. A defect in jurisdiction "in the narrow sense" is thus distinguished from other errors - such as a breach of a duty to be fair, considering irrelevant evidence, acting for an improper purpose, or reaching an unreasonable result - which take place *after* the delegate has lawfully started its activity, but which cause it to leave or exceed its jurisdiction.
>
> ...
>
> It is important to remember that virtually all grounds for judicial review of administrative action depend upon an attack on some aspect of the delegate's jurisdiction (in the wider sense) to do the particular activity in question. Consequently, it is equally important to remember that any behaviour which causes the delegate to *exceed* its jurisdiction is just as fatal as any error which means that it never had jurisdiction "in the narrow sense" even to commence the exercise of its jurisdiction [Italics in original; footnotes omitted.]

[37] It is in the last sense of jurisdiction, as described above, that I understand the issue in this case. The Applicants argue that, while the Board may have had the authority to consider the fact that there was a tax refund, the Board *exceeded* its jurisdiction in making the directions it did. The standard of review for this is, as I

have said, correctness. If, however, the Board did not exceed its jurisdiction, the question then is whether these directions fall within the range of reasonable outcomes.

Submissions on the Appeal:

[38] The essence of the Applicants' argument is that the directions amount to retroactive ratemaking since they were made in the context of the 2008-2010 test years rate application whereas the tax refund applies to a prior year (2007). The 2007 rates were “final” and any attempt to reallocate funds from that period amounts to a revision of those rates. In simple terms, it would require the Applicants to give money received from tax refunds for a prior year to current customers.

[39] The Applicants' argument characterized the directions as an “adjustment” to the utility's revenue requirements for the prior year. How is this? Counsel simplified it for me by explaining that lower taxes means a lower cost base which in turn means lower revenue requirements which results in lower rates. Hence it is an implicit adjustment to the 2007 rate structure to have these funds flow through to the customers.

[40] The Applicants placed great reliance on the Alberta Utilities Commission Decision 2009-215 (referred to previously). In their view that decision addressed exactly the same issues as addressed by the Board in this case and held that any flow through of tax refunds to customers is prohibited by the principle against retroactive ratemaking.

[41] The Intervenors took the position that the Alberta Commission's decision did not deal with the same issues and, even if it did, that Commission came to the wrong conclusions.

[42] In their submission, the income tax deductions claimed by the Applicants have resulted in a reduction of the undepreciated capital cost balances available to offset future taxable income and thus lower income tax expenses. Consequently customers will pay a higher amount of income tax expense through rates in future years. Both the Alberta Commission and the Board in this case came to similar findings in this regard. Counsel for the Intervenors noted that the Board expressly stated that the

customers have been “harmed” and the only way to rectify this is to flow through the tax refunds. Counsel described this as a non-reviewable finding of fact.

[43] The difference as between the Alberta Commission's decision and the Board's, in the Intervenors' submission, is that the Alberta Commission was considering various formulas, such as readjusting capital cost balances, while the Board was dealing with a straightforward cause-and-effect scenario, i.e., the deductions in the past cause harm in the present. Thus it is not an exercise in retroactive ratemaking but prospective ratemaking since it merely restores the integrity of the methodology used to set rates.

[44] Counsel also noted that the Alberta Commission did not simply leave the issue when it decided that it could not order a flow-through of the tax refunds in that case. It directed that a deferral account be established to include all income tax deductible capital costs on a go-forward basis.

[45] The Intervenors' counsel also made the argument that, since these tax refunds were received in 2008, and the Board was considering this issue as part of the 2008-2010 rate application review, it may consider these funds to be part of the revenues of the Applicants for a fiscal period under review (as permitted by s.51(2)(a) of the Act) or as part of the utilities' working capital (as required by s. 49(2)(b) of the Act). Thus there would be no requirement to restate the 2007 cost base or revenue requirements.

[46] Finally, the Intervenors made the point that if utilities keep changing the underlying basis of accounting or tax calculations then there would be no regulatory certainty. In this case, the rates were set on the basis that stock handling charges were 100% capitalized. The utilities have, after-the-fact, changed that to reflect 100% of these costs as tax deductible.

[47] In response, the Applicants point out that any “harm” suffered by current or future customers will be off-set by the fact that customers will benefit from the expensing of these costs since that will lower the amount of taxes payable. So, while the utilities benefit from the deduction taken for 2007, the customers will benefit in the test years and every year thereafter due to the increased tax deductions being claimed by the utilities.

[48] Applicants' counsel also painted the Board's (and the Intervenors') attempt to frame the directions in reference to capital cost allowances and undepreciated capital cost base as merely an attempt to do indirectly what cannot be done directly (a point emphasized by the Alberta Commission in its decision). Any alternative technique or method to either justify or reallocate the refunds to the customers is equally objectionable on this ground.

Analysis:

[49] As I noted earlier, all parties agree that the Board, in exercising ratesetting powers, is required to do so prospectively and is prohibited from engaging in retroactive ratemaking. I think it would be helpful to set out some definitions since various terms are often used interchangeably and in different contexts. In the *Calgary* v. *Alberta* case (*supra*), Hunt J.A. gave a helpful description of the meaning of "prospective", "retroactive" and "retrospective", in the context of utility regulation (at paras. 46-49):

> A brief overview of some central principles of ratemaking, including the related concepts of retroactive and retrospective ratemaking, is necessary. Generally, ratemaking and rates must be prospective: *Coseka Resources Ltd.* v. *Saratoga Processing Co.* (1981), 31 A.R. 541 at para. 29, 16 Alta. L.R. (2d) 60 (C.A.). A utility's past financial results can be used to forecast future expenses, but a regulator cannot design future rates to recover past revenue deficiencies: *Northwestern Utilities Ltd. and al.* v. *Edmonton*, [1979] 1 S.C.R. 684 at 691 and 699 *("Northwestern Utilities"*).
>
> Retroactive ratemaking "establish[es] rates to replace or be substituted to those which were charged during that period": *Bell Canada* v. *Canada (Canadian Radio-Television and Telecommunications Commission*), [1989] 1 S.C.R. 1722 at 1749 ("*Bell Canada 1989*"). Utility regulators cannot retroactively change rates ("*Stores Block"* at para. 71) because it creates a lack of certainty for utility consumers. If a regulator could retroactively change rates, consumers would never be assured of the finality of rates they paid for utility services.
>
> Retrospective ratemaking, in contrast, imposes on the utility's current consumers shortfalls (or surpluses) incurred by previous generations of consumers. It is generally prohibited because it creates inequities or improper subsidizations as between past and present consumers (who may not be the same)...

> Sometimes *retrospective* ratemaking is referred to as *retroactive* ratemaking. This is because rates imposed on a future generation of consumers, while prospective, create obligations in respect of past transactions, and in this sense they are retroactive...

[50] The *Calgary* case also illustrates, in its review of pertinent jurisprudence, that the only way in which expenses or surpluses from one year can be reallocated in a subsequent year, or rates can be changed after-the-fact, is by use of deferral accounts or interim rates. Neither applies in this case, as I previously mentioned.

[51] What the present case demonstrates are aspects of both "retrospective" and "retroactive" ratemaking, as those terms are used above. "Retrospective" because the Board, by its directions, is benefitting present customers from a gain incurred in a past year. "Retroactive" because, in taking the refunds away from the utilities and passing them on to the customers, the Board is in effect restating the utilities' rate base and revenue requirement for that past year.

[52] The Board itself seemed to recognize these principles in an earlier decision, number 4-2008 issued on January 30, 2008, dealing with an issue from the review of the Northwest Territories Power Corporation's 2006-2008 rate application. There, the Board issued a directive requiring the Corporation to refund to customers $345,000 that was, in the Board's term, "over-collected"for certain expenses between the 2001-2002 and 2005-2006 test year periods. As I understand it, the Board asserted that the Corporation had claimed certain expenses when setting the rates for those years but did not carry out all the work related to those expenses, resulting in savings in those years but the potential for higher expenses in future years when the work has to be done. The Corporation asked the Board to review this direction. In its decision, the Board vacated the direction "as a matter of law" after reviewing submissions regarding retroactive ratemaking.

[53] To start, I do not accept the Intervenors' argument that, just because the tax refunds were received in 2008, they can be considered by the Board as revenues applicable to the fiscal year for which the Board is considering setting rates. The amounts are directly referable to operations in 2007 and not to the test years under consideration by the Board. Similarly, the consideration of the working capital of the

utilities is the need to consider the “necessary” working capital for the period in question, not what may simply be available.

[54] Since much emphasis was placed in argument on the Alberta Utilities Commission Decision 2009-215, I will review it in more detail.

[55] The Alberta decision was made in the context of ATCO Electric's application for approval of its 2009-2010 general tariff. In it ATCO identified the retention of income tax refunds, as a result of deductions for various costs (including stock handling charges), for 2006, 2007 and 2008 in the amount of $6 million. These costs were previously treated as capital additions for income tax purposes and formed part of the undepreciated capital cost which was then available to lower taxable income over a period of years through a yearly capital cost allowance deduction. In late 2007, however, ATCO became aware of the ability to deduct these items. Once that was identified, ATCO included provision for these deductions in its 2009-2010 tariff application.

[56] Various consumer groups intervened on the rate application and argued that, in order to receive the refunds, the undepreciated capital cost balances were reduced by the amount of the deductions thereby reducing the capital cost allowance in future years. These groups therefore asked that either the $6 million be flowed through to customers, or that the undepreciated capital cost balance be set at the level existing prior to ATCO's claim for the refunds, or that an adjustment be made to the rate base for 2009-2010.

[57] ATCO argued that all of these methods would amount to retroactive ratemaking since it would involve the Commission in adjusting or restating prior years' revenue requirements after the rates for those years had already been fixed. ATCO also argued, as the Applicants do here, that customers benefit in the long term due to its ability to take these deductions in future years.

[58] As I mentioned previously, the Alberta Commission considered the principle of prospectivity, the prohibition against retroactivity, and the need for regulatory certainty, and allowed ATCO to keep the money realized as a result of these deductions. The Commission held that these principles would be undermined if the refunds were to be paid to customers. It reasoned that the rates were finalized for the

years to which the refunds related and all the alternatives considered were simply a mechanism to reallocate the refunds. Also, to make any of the adjustments proposed by the consumers would be simply doing indirectly what could not be done directly.

[59] The Commission acknowledged that, yes, the customers may have lost some benefit as a consequence of ATCO claiming the deductions but to do as the consumer groups proposed would offend the well-established regulatory principles previously mentioned. It referred to past situations to show that issues arising from the difference in treatment of capital versus expense as between tax and regulatory accounts are not new. And, the Commission also commented on the difference between the tax regime, where there may be reassessments and retroactive changes, and the regulatory regime where certainty is the norm (at para. 68):

> The Commission notes the conflicting incentives and imbalance that arise between shareholders and customers when customer rates are finalized but income tax reassessments and refunds may be requested and received by a utility outside of the test years. While the income tax legislation and its regulations allow for retroactive changes to be made in the calculation of income tax expense resulting in an income tax refund to the benefit of shareholders, the Commission must adhere to the principle against retroactive ratemaking, the prospectivity principle and the principle of regulatory certainty.

[60] In my opinion, the issues addressed by the Alberta Commission are the same ones that were before the Board in the present case. And, in my respectful view, the Commission was correct in its analysis.

[61] The Board based its decision on what it characterized as a "retroactive change in the methodological underpinnings used in the establishment of prospective rates" and seemed to say that if such a change had an impact on future rates it would be in violation of the principle of prospectivity. I must admit to some difficulty in understanding what exactly the Board is saying if I keep in mind that rates are set within the parameters of an application for specific test years. It is the methodology used to set rates for the test years in question that determines the rates (not some past or potential future methodology).

[62] The Board said, in its decision, that "any potential adjustments to future customer rates to reflect the carry over effects of past deductions (is) not a retroactive

adjustment". I agree. But the point is that the adjustment is done to future rates, not by reaching back to a past year and flowing through benefits from that year to customers in a future rate period.

[63] The 2008-2010 application before the Board took into account the potential savings from the deductions that the Applicants are now able to take. Whether those savings actually off-set the reduction in available capital cost allowances is not the point (and the evidence on this was far from clear). The point is that the methodology used in the rate application under consideration is consistent with the changes in tax treatment and internally consistent.

[64] I agree with the Intervenors' counsel when he argues that the 2007 tax refunds cannot be considered as an "efficiency gain". They came about due to a change in federal tax policy as opposed to any efficiencies introduced by the utilities. But, if it is a windfall then the solution is not to provide one to the 2008-2010 customer base. The solution is to concentrate on developing appropriate rates for the test years based on current knowledge.

[65] Any attempt to deal with the refunds received for 2007 within the context of the 2008-2010 rate application is, in my opinion, tantamount to retroactive ratemaking. Calling it a "prospective adjustment" is merely doing indirectly what cannot be done directly. It is axiomatic that the courts will look to the substance of what is being done, and not merely the form, and strike down any attempt to do indirectly what a tribunal's enabling statute does not allow to be done directly: see, for example, *Reference re Agricultural Products Marketing Act*, [1978] 2 S.C.R. 1198 (at p. 1291).

[66] It may well be, as the Intervenors' counsel suggested, that the Board in this case, as opposed to what was done in the Alberta case, was trying to strike a better balance between the interests of consumers and those of the utilities. The difficulty is that in its attempt to do so the Board exceeded its jurisdiction by engaging in what I previously described as both retroactive and retrospective ratemaking.

Conclusions:

[67] Leave to appeal is granted and the appeal is allowed. Decision 4-2010 is hereby set aside and an order will issue granting variance of Board Decisions 24-2008 and

25-2008 by vacating the direction to flow through to customers any benefits from tax deductions for stock handling charges in prior years.

[68] On the matter of costs, if the parties are unable to agree they may file written submissions to me within 60 days of the date of these reasons for judgment.

J.Z. Vertes
J.S.C.

Dated this 24th day of November, 2010.

Counsel for the Applicant: Loyola G. Keough

Counsel for the Respondent: John Donihee

Counsel for the Intervenors: Thomas D. Marriott

Docket: S-1-CV-2010000079

IN THE SUPREME COURT OF THE
NORTHWEST TERRITORIES

BETWEEN:

NORTHLAND UTILITIES (YELLOWKNIFE) LIMITED and NORTHLAND UTILITIES (NWT) LIMITED

Applicants

- and -

NORTHWEST TERRITORIES PUBLIC UTILITIES BOARD

Respondent

- and -

CITY OF YELLOWKNIFE and
TOWN OF HAY RIVER

Intervenors

REASONS FOR JUDGMENT OF
THE HONOURABLE JUSTICE J.Z. VERTES